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Foreign Direct Investments Into the European Union

The Effect of Regulation (EU) 2019/452 on Foreign Investors

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Summary

Foreign direct investments into the EU creates jobs and brings in capital and expertise from all over the world. However, foreign direct investments are not without risks as they can also cause threats to public policy or security in the Union. To mitigate these risks, the EU regulation 2019/452 of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union was implemented ('Regulation'). The Regulation enables Member States to adopt, amend and maintain mechanisms for screening of foreign direct investments within their territory based on the grounds of public order or security. Thus, the Regulation implements a completely new area of EU law which naturally raises questions regarding how the Regulation will affect actors in the area.

To clarify the existing legal framework, this thesis has examined which investments are within the scope of the Regulation and what challenges the Regulation may present for foreign investors active in M&A. It is contended that the scope of the Regulation includes direct investments by third-country nationals or companies registered in a third country. Likewise, the Regulation also enables Member States to screen investments by companies incorporated in the EU or nationals of the EU if certain requirements are met.

Furthermore, regarding potential challenges for foreign investors this thesis concludes that it is uncertain what investments may cause threats against public order or security as the grounds have not been clearly defined in the legal framework. Additionally, more guidance is needed regarding the factors which the Member States are encouraged to consider or to take into account when determining if a foreign investment is likely to affect public order or security. To summarize, further guidance is needed from the Commission, the Member States and the CJEU.

This thesis concludes that the cooperating mechanism, which follows from the Regulation, can affect foreign investors as national authorities of Member States may feel obligated to act in accordance with comments from other Member States or opinions by the Commission. Moreover, due to the cooperation mechanism, sensitive information may become available to up to 28 contact points which can give rise to concern for the protection of such information.

In conclusion, this thesis finds that the questions that remain regarding the legal framework increases uncertainty for foreign investors which decreases transaction certainty.

In addition, this thesis has also examined if Chinese investors are particularly exposed to the challenges presented by the Regulation. The conclusion of this thesis is that such is the case, for instance due to the close ties between the Chinese government and Chinese companies and the political

challenges facing Chinese investors in the EU. Therefore, M&A-deals with Chinese investors may contain more closing conditions which decreases transaction certainty further. As transaction certainty can influence what offers are accepted, this circumstance may put Chinese investors at a disadvantage during bidding.

Sammanfattning

Utländska direktinvesteringar i EU skapar arbetstillfällen och för med sig kapital samt expertis från hela världen. Utländska direktinvesteringar är dock inte helt utan risk då de även kan ge upphov till hot mot säkerheten eller allmänna ordningen i unionen. I syfte att hantera dessa risker antogs förordning (EU) 2019/452 av den 19 mars 2019 om upprättande av en ram för granskning av utländska direktinvesteringar i unionen. Förordningen möjliggör för medlemsstaterna att anta, ändra eller behålla system för granskning av utländska direktinvesteringar inom medlemsstaternas territorium med hänsyn till allmän ordning eller säkerhet. Därigenom skapar förordningen ett nytt rättsområde inom EU-rätten vilket naturligtvis väcker frågor om hur förordningen kommer påverka aktörer verksamma inom området.

I syfte att klargöra rättsläget har uppsatsen undersökt vilka investeringar som faller inom förordningens tillämplighetsområde samt om förordningen kan ge upphov till utmaningar för utländska investerare aktiva inom företagsförvärv.

Uppsatsens slutsats är att förordningens tillämplighetsområde inkluderar direktinvesteringar av tredjelandsmedborgare eller företag registrerade i ett tredjeland. Vidare inkluderar förordningens tillämplighetsområde även direktinvesteringar av medborgare i EU eller företag registrerade i EU, om särskilda förutsättningar är uppfyllda. Gällande frågan om förordningen ger upphov till utmaningar för utländska investerare har uppsatsen funnit följande. Det är osäkert vilka transaktioner som kan ge upphov till hot mot den allmänna ordningen eller säkerheten eftersom dessa begrepp inte är klart definierade inom rättsområdet. Vidare krävs mer vägledning rörande de faktorer som medlemsstaterna uppmuntras överväga eller beakta vid fastställandet av om en utländsk direktinvestering kan påverka den allmänna ordningen eller säkerheten. Sammanfattningsvis finns ett behov av vägledning från EU-kommissionen, medlemsstaterna och EU-domstolen.

Därutöver har uppsatsen funnit att samarbetsstrukturen som följer av förordningen kan påverka utländska investerare då medlemsstaterna kan känna sig förpliktigade att följa synpunkter från andra medlemsstater eller yttranden från kommissionen. Vidare följer av samarbetsstrukturen att känslig information kan bli tillgänglig för upp till 28 kontaktpunkter vilket kan ge upphov till oro över skyddet av sådan information.

Sammanfattningsvis finner uppsatsen att de frågor som kvarstår om rättsläget leder till en ökad osäkerhet för utländska investerare vilket minskar transaktionssäkerheten för dem.

Vidare har uppsatsen undersökt om kinesiska investerare är särskilt utsatta för de utmaningar som förordningen kan ge upphov till. Slutsatsen är att så är fallet, bland annat på grund de starka banden mellan den kinesiska staten och kinesiska företag samt de politiska utmaningar som kinesiska investeringar möter i EU. Därav kan M&A-affärer med kinesiska investerare komma att inkludera fler villkor i avtalen vilket minskar transaktionssäkerheten. Eftersom transaktionssäkerheten kan påverka vilka bud som accepteras kan denna omständighet sätta kinesiska investerare i underläge vid budgivning.

Preface

The years I have spent at Lund University have truly inspired me and challenged me to grow as an individual. However, I could not have made it this far alone. Therefore, I would like to thank my family and friends for supporting me on this journey. Furthermore, I would like to specially thank Daria Davitti for all your help and positivity and Julian Nowag for encouraging me to write about a subject that interests me. I would also like to thank all of department four of Malmö district court as well as my colleagues at Malmö administrative court, you have taught me so much and for that I am forever grateful.

Abbreviations

China	People's Republic of China
Commission	European Commission
CJEU	Court of Justice of the European Union
EU	European Union
IMF	International Monetary Fund
M&A	Mergers and acquisitions
OECD	The Organization for Economic Co-operation and Development
SOE	State-owned enterprise
SPA	Share or asset purchase agreement
SPE	Special-Purpose Entities
UNCTAD	United Nations Conference on Trade and Development

1 Introduction

This thesis examines foreign direct investments ('FDI') into the European Union ('EU'), in the form of acquisitions of shares in European enterprises by foreign investors.

1.1 Bakground of the Research

The subject of foreign direct investments into the EU has been a topic of interests in both political and legal debates. In 2016 several high-profile take-overs of European enterprises were attempted or completed by investors from the People's Republic of China ('China'). These bids were met with some concern from both the affected industries and politicians.[1] At the end of 2016, the Swedish Ministry of Defense published a report on Chinese acquisitions in Europe and their strategic implications which illustrated the growing concern over Chinese outbound investments. Concerns were especially raised over the increased acquisitions of enterprises of strategic value due to concerns for national security and competitiveness.[2] Furthermore, politicians were growing agitated over the lack of reciprocity in regard to European investments in the Chinese market.[3] In February 2017, Germany, France and Italy came together to present a joint letter to the European Commissioner for Trade. The letter called for discussions at European level on the challenges brought by FDI in the EU from third country investors.[4] Shortly thereafter the European Commission ('Commission') recognized the aforementioned concerns in its Reflection Paper issued on 10 May 2017 on 'Harnessing Globalization':

> Openness to foreign investment remains a key principle for the EU and a major source of growth. However, concerns have recently been voiced about foreign investors, notably state-owned enterprises, taking

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1 G. Parker and L. Hornby, 'Hinkley Point review signals UK rethink on Chinese investment', Financial times, 29 July 2016; G. Chazan, 'German angst over Chinese M&A', Financial times, 9 August 2016; P. Mozur and J. Ewing 'Rush of Chinese Investment in Europe's High-Tech Firms Is Raising Eyebrows', The New York Times, 16 September 2016.

2 J. Hellström, 'China's Acquisitions in Europe', Ministry of Defense, December 2016, FOI-R--4384—SE.

3 Commission, 'Joint communication to the European Parliament and the Council, Elements for a new EU strategy on China' JOIN (2016) 30 final, pp. 4 and 8; See also P. Taylor, 'Chinese investment welcome in France... up to a point', *Reuters,* 8 June 2016.

4 B. Zypries, M. Sapin and C. Calenda, 'Proposals for ensuring an improved level playing field in trade and investment' [letter to Commissioner C. Malmström], February 2017.

> over European companies with key technologies for strategic reasons. EU investors often do not enjoy the same rights to invest in the country from which the investment originates. These concerns need careful analysis and appropriate action.[5]

Just a few months thereafter, the Commission presented a proposal for a regulation establishing a framework for screening of FDI into the EU.[6] Finally, two years later, the EU regulation 2019/452 of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union ('Regulation') was implemented. The Regulation, which entered into force on 11 October 2020, is binding in its entirety and directly applicable in all Member States.[7] Despite the implementation of the new Regulation, concerns over FDI into the Union have not subsided. In fact, the current global pandemic seems to have raised concerns once again over takeovers of European companies by third country investors. This worrisome new outlook is for instance demonstrated by the Commission urging Member States to implement FDI screening mechanisms.[8]

While it may appear as though the Commission has a negative outlook on FDI, the Regulation does in fact recognize the contribution of FDI to the economy of the Union. Indeed, FDI into the Union generates jobs and brings in capital along with technologies from all over the world. Although FDIs can take different forms, 67 percent of the total deal value of FDI into the EU in 2003-2016 was made up of mergers and acquisitions ('M&A') at a total deal value of 1,700 billion euros.[9]

Traditionally, the influx of FDI has originated from countries with advanced economies, such as Switzerland, the US and Japan. However, in the last few years China has emerged as a new investor into the EU. Since the beginning of the 21st century, China has gone from being a virtually non-existent player in the field of FDI into the EU, to growing exponentially and

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[5] Commission, 'Reflection paper on harnessing globalization' COM (2017) 240 of 10 May 2017, p. 15.

[6] Commission, 'Proposal for a regulation of the European parliament and of the council establishing a framework for screening of foreign direct investments into the European Union' COM (2017) 487 final.

[7] Article 17 the Regulation.

[8] Commission, 'Guidance to the Member States concerning foreign direct investment and free movement of capital from third countries, and the protection of Europe's strategic assets, ahead of the application of Regulation (EU) 2019/452 (FDI Screening Regulation)' (Communication) C (2020) 1981 final.

[9] E. Rytter Sunesen, and J. Juul Henriksen, 'The Economics of FDI Screening' in Bourgeois, J HJ. (ed.) *EU Framework for Foreign Direct Investment Control*, Kluwer Law International BV., 2020, p. 4.

establishing itself as one of the top upcoming players.[10] China's exponential growth is for example demonstrated by the growing number of companies under Chinese control. In 2007, China[11] only controlled around 5 000 firms in the EU, and just 10 years later, in 2017, that number had risen to more than 28 000.[12] That same year, in 2017, China[13] accounted for 6.5 percent of all M&A deals in the EU by foreign investors.[14]

Chinese investments into the EU started to rise during the euro crisis when the EU was experiencing drops in direct investments by other foreign investors.[15] Due to the challenges many Member States were facing at the time, the inflow of FDI from China was largely welcomed by politicians. However, as previously mentioned, a few years later several Chinese investments in the EU ended up in the political spotlight which ignited debates over the political implications of Chinese investments. Even so, the attitude towards Chinese investments remained overall positive within the EU.[16] However, at the beginning of 2020, a new corona virus pandemic swept over the Member States and shocked the Union, as well as the rest of the world, to the core. Due to the effect of the virus on the economy of the EU, the Commission identified an increased risk of takeovers of companies in sensitive sectors by foreign investors. In order to minimize this risk, the Commission urged Member States to make full use of existing FDI screening mechanisms and implement fully fledged screenings.[17] This leads us to the present situation, where the Regulation has entered into force and the Member States have been urged to implement FDI screening mechanisms. The present situation indicates that more and more Member States will implement FDI screening mechanisms at a time where the legal framework regarding FDI has not yet been fully established through court practice from the Court of Justice of the European Union ('CJEU') or by legal experts and scholars. Hence, foreign investors may be in for a time of uncertainty. As there is research that

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[10] Commission, 'Foreign direct investment in the EU. Following up on the Commission Communication "*Welcoming Foreign Direct Investment while Protecting Essential Interests*" of 13 September 2017' SWD (2019) 108 final, p. 1.

[11] Along with Hong Kong and Macao.

[12] SWD (2019) 108 final, p. 13.

[13] Along with Hong Kong and Macao.

[14] SWD (2019) 108 final, p. 15, figure 2.7.

[15] S. Meunier, ''Beggars can't be Choosers': The European Crisis and Chinese Direct Investment in the European Union', *Journal of European Integration*, vol. 36, no. 3, 2014, p. 287.

[16] S. Meunier, 'Beware of Chinese Bearing Gifts', in J. Chaisse (ed.), *China's International Investment Strategy: Bilateral, Regional, and Global Law and Policy*, Oxford University Press, 2019, pp. 355-356.

[17] C (2020) 1981 final.

suggests that uncertainty surrounding government policies can negatively affect M&A activity, it is important to minimize such uncertainty.[18]

To summarize, it is known that FDI into the EU stimulates the economy. The majority of the total deal value of FDI into the EU are from M&A deals. Chinese investors are a relatively new form of investors in the EU and have proven quite controversial because of the potential takeover of sensitive sectors.

In conclusion, it is important for the economy of the EU to retain the interest of foreign investors. Moreover, as M&A deals account for the majority of the deal value of FDI into Europe, it is important to retain the interest of foreign investors to acquire or merge with companies in the EU. So how can the EU retain the interest of foreign investors? As previously mentioned, M&A deals may be negatively influenced by policy uncertainty. Therefore, the EU and the Member States may be able to retain the interest of foreign investors by minimizing policy uncertainty. To minimize such uncertainty, the legal framework established by the Regulation must be analyzed and clarified. In other words, foreign investors must be able to understand if they will be affected by this new Regulation and if so, how. Furthermore, as China is an up-and-coming player in the international investment field, it is interesting to consider whether Chinese investors are particularly affected by this new legal framework due to the controversy outlined above.

1.2 Purpose and Research Questions

The novelty of the Regulation means that it is still uncertain how the Regulation will affect foreign investors in the EU. Therefore, foreign investors wishing to invest in the EU may encounter policy uncertainty which can negatively affect M&A activity. To maintain the interest of foreign investors in the EU, this uncertainty must be minimized. Therefore, the purpose of this thesis is to minimize policy uncertainty due to the Regulation by examining which investments are subject to the Regulation and what challenges the Regulation may present for foreign investors investing into the EU. To fulfil this purpose, the following research questions will be examined:

I. Which investments are subject to the Regulation?
II. What challenges may the Regulation present for foreign investors?
III. Are Chinese investors particularly exposed to such challenges?

[18] N. H. Nguyen and H. V. Phan, 'Policy Uncertainty and Mergers and Acquisitions', *Journal of Financial and Quantitative Analysis*, vol. 52, no. 2, 2017, p. 613; A. Bonaime, H. Gulen and I. Mihai, 'Does policy uncertainty affect mergers and acquisitions?', *Journal of Financial Economics*, vol. 129, no. 3, 2018, pp. 553-554.

1.3 Delimitation

Due to the limited length required for this work, this thesis will only examine FDI in the form of acquisitions of shares or voting power in companies. The reason for this is that M&A deals account for the majority of the deal value of FDI into the Union by foreign investors. Therefore, neither greenfield investments nor other types of direct investments beyond M&A deals are examined. Moreover, this thesis will not be examining screening of capital movements that are not in the form of direct investments, such as portfolio investments.

Furthermore, only the exception from the free movement of capital stipulated in article 65(1)(b) Treaty on the Functioning of the European Union ('TFEU') will be discussed as this exception is, in the opinion of this thesis, the most important in the context of the Regulation.[19] Moreover, this thesis will not examine the relationship between foreign direct investments and the freedom of establishment as this thesis primarily focuses on *foreign* investors. Finally, this thesis will not examine bilateral investment treaties. These delimitations have been implemented due to constraints allotted this work, such as time and length.

1.4 Method: Doctrinal Approach

The aim of this thesis is to determine the applicable law of the Regulation and analyse what challenges the Regulation may present for foreign investors. This thesis attempts to establish the applicable law of the Regulation through a doctrinal method. The doctrinal method that was used is known in Sweden as the legal dogmatic method.

The role of the legal dogmatic method is to describe the applicable law as it follows from general sources of law. This is done by interpreting and determining the law as it exists ('lex lata') and systemizing lex lata in the form of principles, rules and legal literature.[20] The sources of utmost influence in this regard are the following, in order of importance:

i. *primary legislation* such as EU Treaties and the general principles established by the Court of Justice of the European Union ('CJEU'),
ii. *secondary legislation* such as regulations, directives, decisions, recommendations, opinions, communications, resolutions and white papers,

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[19] Consolidated version of the Treaty on the Functioning of the European Union [2012] OJ C326/47 ('TFEU').

[20] C. Sandgren*, Rättsvetenskap för uppsatsförfattare: Ämne, material, metod och argumentation*, 4th edn., Stockholm, Nordstedts Juridik AB, 2018, p. 49.

iii. international agreements, and
iv. *supplementary sources of law* such as the case practice of the CJEU and international law.[21]

Furthermore, the application of these sources of law in legal literature will be examined as to interpret and determine lex lata.

However, this thesis does not only attempt to determine lex lata but also to analyse how the Regulation may affect foreign investors and what challenges may arise. In the analysis, this thesis used the doctrinal approach of the legal analytical method,[22] as defined by Claes Sandgren. According to Sandgren, the purpose of the legal analytical method is both to determine lex lata and to analyse it. In doing so, this method utilizes far more sources of law than the legal dogmatic method.[23] Thus, when analysing what challenges the Regulation presents for foreign investors, this thesis will examine sources beyond the traditional legal sources. Such sources will be carefully selected to ensure the highest possible level of understanding and clarification of the existing legal frameworks.

1.5 Literary Review

Before the implementation of the Regulation, FDI screening mechanisms were not regulated at EU level.[24] Therefore, this is a relatively new area of EU law which means, in turn, that case law and legal literature determining the scope of the Regulation are relatively scarce in relation to FDI screening mechanisms. With that said, the Commission has published relevant documentations, such as working documents and communications on FDI screening mechanisms.[25] As illustrated in the previous section, recommendations, opinions, communications, and white papers are sources of secondary legislation of EU law. Thus, this thesis considers them to be high value sources for the determination of EU law. Furthermore, this thesis considers the opinion of Professor Steffen Hindelang in *The Free Movement of Capital and Foreign Direct Investment: The Scope of Protection in EU Law* (2009) to be relevant in the determination of EU law as the literature

[21] The Publication Office of the European Union, EUR-Lex, 'Sources of European Union law' [website].
[22] In Swedish 'Rättsanalytisk metod'.
[23] Sandgren, *Rättsvetenskap för uppsatsförfattare*, pp. 50–52.
[24] With that said, certain Member States already had FDI screening mechanisms in place.
[25] SWD (2019) 108 final; Commission, 'Welcoming Foreign Direct Investment while Protecting Essential Interests' COM (2017) 494 final; C (2020) 1981 final.

examines FDI in EU law.[26] Hindelang's monograph, although authoritative, is superseded by the Regulation by a decade which may lead to doubts regarding its applicability to the Regulation. However, this thesis has found that Hindelang's findings are supported by the case law of the CJEU as well as primary and secondary legislation of the EU. Therefore, as the Regulation should be interpreted with regards to these other sources of law, the work is applicable to the Regulation regardless of its date of publishing. Nevertheless, the age of the work must be considered in the interpretation of its findings. Furthermore, this thesis has examined the work of international organizations which have close ties to the EU and whose work have been recognized by the Commission. With that said, it is important to note that the work of these organizations is not considered to be a general source of law of the EU.

As for the part of this thesis that aims to analyze the effect of the Regulation on foreign investors, this thesis will, along with previously mentioned sources, examine the opinions of scholars and lawyers active in the fields of M&A and investment law. In doing so, this thesis will primarily examine sources published in international law journals. However, in this regard it is important to note that the opinions expressed by these scholars are not general sources of EU law and may, in the worst case, be affected by the authors' political opinions. With that said, this thesis considers them of value for the interpretation of the Regulation and the challenges it may present for foreign investors.

1.6 Outline

First and foremost, foreign investors must be made aware of whether their investment is subject to the Regulation or not. Therefore, chapter two of this thesis examines what investments are as well as which types of investments and investors are subject to the Regulation. Secondly, it is important to minimize uncertainty regarding the new legal framework. Therefore, chapter three examines the Regulation as well as the challenges it may present for foreign investors. Furthermore, the chapter also examines what affects the Member States decision to screen FDI and screening decisions. Thirdly, due to the current controversy regarding Chinese investments in the EU, it is important for Chinese investors to be aware of how this controversy will affect their investments into the EU. Accordingly, chapter four of this thesis examines if the Regulation may affect Chinese investors more than other types of investors. The findings of this thesis are analyzed throughout and

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[26] S. Hindelang, *The Free Movement of Capital and Foreign Direct Investment: The Scope of Protection in EU Law*. Oxford, Oxford university press, 2009.

each of chapters two to four ends with a preliminary analysis which discusses and presents the preliminary conclusions of said chapter. Lastly, chapter five will discuss and draw conclusions from the overall findings of this thesis.

2 Investments

In order to minimize policy uncertainty, foreign investors must be able to understand and predict when their investments will be subject to the Regulation. Therefore, the definition of a foreign direct investment must be established. As a means to examine the definition of a foreign direct investment, the concept of investments must first be examined. In simple terms, an investment can be explained as the act of putting money into something in order to make a profit. In the case of acquisitions of shares in enterprises, the investor purchases shares in target companies. As such, the investor receives shares in the target company in exchange for something of equal value. In other words, a transaction takes place where *capital*, either real or financial, *moves* from one party to another. Thus, investments are the movement of capital, i.e. capital movements. As foreign direct investments are a type of investment, it follows that they are also capital movements.[27] Therefore, the legal framework for capital movements is applicable to foreign direct investments.

While not all capital movements are foreign direct investments, all foreign direct investments are capital movements. Thus, to determine if an investment is within the scope of the Regulation, we must understand what distinguished FDI from other types of movements of capital. Therefore, we must first examine the movement of capital.

2.1 Movement of Capital

Capital movements between different Member States or between Member States and third countries are protected by the free movement of capital regulated in article 63 TFEU.[28] Thus, any restrictions against third-country capital movements are prohibited. As follows from case law of the CJEU, the prohibition against restrictions on the movement of capital goes beyond the elimination of unequal treatment on grounds of nationality.[29] Instead, the prohibition contains two guarantees: first, the prohibition against hindrance

[27] COM (2017) 487 final, p. 4.

[28] TFEU, art 63.

[29] Judgement of 4 June 2002, *Commission v Portugal*, C-367/98, EU:C:2002:326, para 44.

of access to the market,[30] second, the prohibition of discrimination.[31] In essence, all national measures that are likely to deter investors from other Member States from investing or limit or prevent the acquisition of shares in a company shall be regarded as restrictions.[32] However, there are exceptions to the prohibition against restrictions on capital movements which are regulated in articles 64-66 TFEU. Of these, the exception in article 65(1)(b) is of interest in the context of the purpose of this thesis:[33]

> The provisions of Article 63 shall be without prejudice to the right of Member States: […] to take measures which are justified on grounds of public policy or public security.[34]

In other words, Member States may restrict the free movement of capital on grounds of public policy or public security. See more on public policy or public security in section 3.3. For now, let us continue to examine the movement of capital.

It is the *movement* of capital that is protected by the article, not the capital in itself. This means that all necessary action for the purpose of moving the capital are protected against restrictions. Furthermore, the freedom is only applicable to capital movements with a cross-border dimension. To put it differently, the freedom is applicable to capital movements that extends across national borders.[35] Since capital does not necessarily have a physical location we must first establish where it is located in order to examine if the movement extents across national borders. According to Hindelang, real property and capital goods are located where they are situated or stored, whilst intangible capital is located where the holder of the capital is located. Moreover, the holder of the capital is located at their habitual residence or in other words, where they ordinarily stay. Regarding the residency of legal persons, Hindelang suggests that a legal person resides in the state to which it shows a continuous and effective link to the economy

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[30] Judgement of 24 November 1993, *Bernard Keck v Daniel Mithouard*, C-267/91 and C-268/91, EU:C:1993:905, para 16; See also judgment of 14 November 1995, *Svensson and Gustavsson v Ministre du Logement and de l'Urbanisme*, C-484/93, EU:C:1995:379, para 10.

[31] Judgement of 24 June 1986, *Luigi Brugnoni and Roberto Ruffinengo v Cassa di Risparmio di Genova e Imperia,* C-157/85, EU:C:1986:258, para 17; Judgement of 14 March 2000, *Association Église de Scientologie de Paris Scientology International Reserves Trust v The Prime Minister*, C-54/99, EU:C:2000:124, para 3; See also Hindelang, *The free movement of capital and foreign direct investment,* p. 115.

[32] Judgement of 23 October 2007, *Commission v Germany,* C-112/05, EU:C:2007:623, para 19.

[33] COM (2017) 487 final, p. 4.

[34] TFEU, art 65(1)(b).

[35] Hindelang*, The free movement of capital and foreign direct investment,* pp. 58-59.

of said state.[36] It follows from the case law of the CJEU that the cross-border context should be interpreted broadly.[37]

Now that the location of capital has been explained, let us examine the concept of 'movement of capital' more closely. Article 63(1) TFEU does not define the term 'movement of capital' and Hindelang argues that the term does not have a definite meaning. Thus, we must turn to secondary sources of law in order to understand the term. From the jurisprudence of the CJEU follows that Annex I to Council Directive 88/361 EEC of 24 June 1988 for the implementation of Article 67 of the Treaty reveals by way of example the scope of the free movement of capital:[38]

> […] the nomenclature in respect of movements of capital annexed to Directive 88/361 still has the same indicative value, for the purposes of defining the notion of capital movements, […] subject to the qualification, contained in the introduction to the nomenclature, that the list set out therein is not exhaustive.[39]

As follows from Annex I, capital movements listed in the Nomenclature include, inter alia, direct investments on national territory by non-residents and direct investments abroad by residents. Thus, direct investments are capital movements which, when the investment has cross-border links, are protected from restrictions in accordance with article 63(1) TFEU.

To summarize, capital movements that have a cross-border link may be protected against restrictions by the free movement of capital. Direct investments are capital movements and are therefore protected against restrictions with exceptions. Now that the basics of capital movements have been explained, let us examine the concept of direct investments.

2.1.1 Direct Investments

As established in the previous section, direct investments are movements of capital and therefore, as a principal rule, protected against restriction by the free movement of capital. As a way of further clarification, let us examine the following metaphor. Roses, dandelions and geraniums are all different varieties of flowers. They look different, smell different and even sometimes

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[36] Hindelang, *The free movement of capital and foreign direct investment,* pp. 48-52 and 58-59.

[37] Judgement of 26 September 2000, *Commission v Kingdom of Belgium,* C-478/98, EU:C:2000:497, para 16

[38] Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty [1988] OJ L 178/5; Hindelang, *The free movement of capital and foreign direct investment,* p. 44.

[39] Judgement of 16 March 1999, *Manfred Trummer and Peter Mayer,* C- 222/97, EU: C:1999:143, para 21.

require different types of soils. One would never mistake a dandelion for a rose and yet, they are both flowers. In the same way, capital movements can be thought of as the umbrella term covering different types of capital movements just like the term flower covers different types of flowers. In this way, direct investments are capital movements just like roses are flowers. Therefore, we must examine what distinguishes direct investments from other types of capital movements.

When establishing the concept of 'direct investments', the CJEU has referred to the nomenclature of the capital movements as set forth in Annex I of Directive 88/361 as well as the explanatory notes therein.[40] The explanatory notes defines direct investments as:

> Investments of all kinds by natural persons or commercial, industrial or financial undertakings, and which serve to establish or to maintain lasting and direct links between the person providing the capital and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity. This concept must therefore be understood in its widest sense.[41]

From this follows that direct investments are those which serve to *establish or maintain lasting and direct links in order to carry out economic activity*. Furthermore, Annex I contains examples of direct investments, of these the following two are of interest in the context of M&A deals:

> 1. Establishment and extension of branches or new undertakings belonging solely to the person providing the capital, and the acquisition in full of existing undertakings.
>
> 2. Participation in new or existing undertaking with a view to establishing or maintaining lasting economic links.[42]

From the first example follows that the acquisition of all the shares in a target company is a direct investment. Thus, to understand if an investment is a direct investment based on this first example, one must simply determine if all the shares in the target company have been acquired or not.

The second example is somewhat trickier. In order to understand if an acquisition of shares in a target company by an investor is a direct investment, one must determine if the investor intended to establish or maintain lasting economic links. Furthermore, as follows from the explanatory notes, the links

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[40] Judgement of 12 December 2006, *Test Claimants in the FII Group Litigation v Commissioners of Inland Revenue*, C-446/04, EU:C:2006:774, paras 178-181, ('*FII Group Litigation*').

[41] Dir [1988] OJ L 178/5, Explanatory Notes, Annex I.

[42] Dir [1988] OJ L 178/5, Annex I.

must be both lasting and direct. What then is the meaning of *establishing or maintaining lasting and direct links*?

According to the jurisprudence of the Court, a direct investment, as determined by the second example in Annex I, presupposes that:

> the shares held by the shareholder enable him, either pursuant to the provisions of the national laws relating to companies limited by shares or otherwise, to participate effectively in the management of that company or in its control.[43]

In other words, an investment has established or maintained lasting economic links when the investment enables the investor to *participate effectively in the management* of the target company or in its *control*. Following this, we must examine when the investor can participate effectively in the management or control of the target company.

In order to demonstrate this relationship, let us briefly return to the first example of direct investments in Annex I.[44] As previously mentioned, if an investor acquires all the shares in a target company, the investment is clearly a direct investment, but why is this the case? The reason for this is quite simple as illustrated by the Opinion of Advocate General Alber:

> since all the shares are owned by one person. The sole owner of all a company's shares can make decisions about that company's activities on his own: there is no-one else entitled to a say whose views he must heed. Only the legal form of the undertaking distinguishes him from a sole trader; like the latter, he is in a position to direct the activities of the business in question.[45]

Even though the Opinion relates to the freedom of establishment, it illustrates that if there is only one shareholder, that shareholder can control the target business as they wish. Thus, effective participation in the management or control of the target business is achieved by that single shareholder.

Now, let us return to example two of direct investments in Annex I, Hindelang claims that the distinctive feature of direct investments is that the investor, through the investment, is placed in a position where they can pursue their entrepreneurial aims.[46] This, he argues, is achieved either by control of the target business or by participation in the management of the target

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[43] *FII Group Litigation*, para 182; See also direct investments, Dir [1988] OJ L 178/5, Explanatory notes, Annex I.

[44] 'Establishment and extension of branches or new undertakings belonging solely to the person providing the capital, and the acquisition in full of existing undertakings', see Dir [1988] OJ L 178/5, Annex I.

[45] Opinion of AG Alber of 14 October 1999, *Baars*, C-251/98, EU:C:1999:502, para 34.

[46] Hindelang, *The free movement of capital and foreign direct investment,* p. 64.

business. According to Hindelang, effective participation in the management of the target business equals actively taking part in everyday tasks of administrative, executive and supervisory direction. Moreover, Hindelang suggests that effective participation in the control of an investment entails influence over the undertaking which can take many forms. Yet, Hindelang argues that the decisive test for when such control is achieved is when the investors consent is necessary for the undertaking of major or important entrepreneurial decisions.[47]

Furthermore, effective participation in the control of the target business can be achieved in different ways, for instance, through majority shareholdings or minority stakes together with the power of veto.[48] With that said, there are no set thresholds at which it can be said that the investor has acquired enough shares or voting rights to achieve control, instead it must be determined on a case-by-case basis with guidance from applicable company laws.[49] See more on effective participation in the management or control of the company in section 2.2.1.

What then if an investor acquires shares in a target company without enabling lasting and direct links as described above? In that case, the investment is not a direct investment but a portfolio investment. Similar to direct investments, portfolio investments are movements of capital. However, unlike direct investments, portfolio investments are made with the sole intention of achieving a financial investment and without influencing the management or control of the company.[50]

To summarize, a direct investment is an investment with the aim of establishing or maintaining lasting and direct links between the investor and the entrepreneur or investment. Such lasting links can be achieved through participation in the management or by control of the target business. In the context of this thesis, only direct investments through the acquisition of shares are of import. Now that the meaning of direct investments has been examined the next step is to examine *foreign* direct investments as per the Regulation.

2.2 Foreign Direct investments

The Regulation defines foreign direct investments as the following:

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[47] Hindelang, *The free movement of capital and foreign direct investment,* pp. 70–71.

[48] Hindelang*, The free movement of capital and foreign direct investment,* pp. 71-72.

[49] Judgement of 13 April 2000, *Baars,* C-251/98, EU:C:2000:205, para 20; Hindelang*, The free movement of capital and foreign direct investment,* pp. 68-71.

[50] Judgement of 28 September 2006, *Commission v. Netherlands*, C-282/04 & C-283/04, EU:C:2006:608, para 19; See also Dir [1988] OJ L 178/5, Annex I.

> an investment of any kind by a foreign investor aiming to establish or to maintain lasting and direct links between the foreign investor and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity in a Member State, including investments which enable effective participation in the management or control of a company carrying out an economic activity.[51]

As per the above definition, a FDI is any investment which aims at establishing or maintaining lasting and direct links between the foreign investor and the entrepreneur or the undertaking. Thus, as illustrated by the previous section, FDIs are a form of direct investments. To illustrate this, let us examine the example of flowers again. We know that roses are flowers, and what we have now learned is that there are different varieties of roses which can have different colours, smells and even grow in different types of climates. In the same way, direct investments are capital movements and foreign direct investments are a sort of direct investments.

As previously mentioned, portfolio investments are not direct investments. Accordingly, they are not subject to FDI screening mechanisms per the Regulation.[52] However, this does not mean that Member States cannot screen portfolio investments. With that said, portfolio investments do not give the investor the possibility to exercise effective influence over the management and control of the target company, and therefore, they ordinarily present less issues with regards to security or public order than FDI.[53] Thus, it is important for foreign investors to understand where the line between direct investments and portfolio investments is drawn. Therefore, the objective of establishing or maintaining lasting and direct links between the investor and the entrepreneur or target company must be further examined.

2.2.1 Direct and Lasting Links

As previously discussed, the objective of establishing or maintaining direct and lasting links can be achieved in two ways. Firstly, through *effective participation in the management* of the target company. Secondly, through *effective participation in the control* of the target company, otherwise known as effective control of the target company. While the intent behind direct investments is to achieve this objective, the opposite is true for portfolio investments.[54] With that said, proving what intention the investor had with

[51] Regulation, art 2(1).
[52] Regulation, preamble 9.
[53] C (2020) 1981 final, p. 2.
[54] *Commission v Netherlands*, para 19.

the investment is hardly possible. Therefore, the intention must be determined by objective criteria. According to Hindelang, the objective is achieved as soon as the investor has the possibility of managing control over economic activities. Thus, it is the *possibility* of control which must be determined, not actually executed control. Furthermore, Hindelang suggests that effective control of an investment is achieved when the consent of the investor, alone or together with others, is needed for important entrepreneurial decisions. [55]

As previously discussed, effective control can be achieved through the acquisition of majority shareholding. However, such control also can be achieved through the acquisition of minority shares, e.g., when coupled with veto rights or through management contracts which grants the investor the influence needed to participate in the control of the target company.[56] Other cases where control can be achieved through minority shares is when the target company has a varied and disorganised ownership structure. Through the acquisition of minority shares in such companies, investors can find themselves with significant influence despite minority shareholdings.[57]

According to Hindelang, there is no set threshold at which it is possible to establish whether the investor has acquired enough shares or voting rights to be in control of the company. Instead, he argues that an examination must be made on a case-by-case basis. Even so, thresholds found in secondary sources of law may yet be of value for investors as they may provide guidance for when the Member States considers that the investor has achieved effective control of the investment through shareholdings. In other words, these thresholds may indicate a threshold of ownership of shares or voting power at which the national authorities of the Member States presumes that the investor has the possibility of control of the investment.[58] Furthermore, the same can be said for the Commission, i.e., these following thresholds may indicate a threshold of ownership at which the Commission presumes that an investor has the possibility of participating effectively in the control of the target company. Therefore, thresholds established in Community law and supplementary sources of law will be examined in order to ascertain when the Member States and the Commission may presume that an investment is a direct investment. The first of these thresholds can be found in Community law in Council Directive 2011/96/EU.[59] For the purpose of Directive 2011/96/EU the status of a parent company is attributed to a company of a

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[55] Hindelang, *The free movement of capital and foreign direct investment,* p. 65 and 74.
[56] Hindelang, *The free movement of capital and foreign direct investment,* pp. 71-72.
[57] SWD (2019) 108 final, p. 51.
[58] Hindelang, *The free movement of capital and foreign direct investment,* p. 71.
[59] Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States [2011] OJ L345/8.

Member State with a minimum holding of 10 percent in the capital of a company of another Member States. The second of these thresholds can also be found in Community law in Council Directive 2013/34/EU.[60] As per the definition of participating interest in article 2(2) of Council Directive 2013/34/EU, the holding of capital in another undertaking is presumed to constitute a participating interest when it exceeds at least 20 percent. Thus, these secondary sources of Community law indicate that links between different enterprises which may enable control can arise around 10-20 percent of shareholding. Accordingly, secondary sources of EU law seem to indicate that a level between 10 and 20 percent of shareholdings by an enterprise in another enterprise usually indicates links between the enterprises.

Furthermore, international organisations have developed benchmarks establishing definitions for direct investments and FDIs based on ownership of shares or voting power in the target company. These may also be of guidance for when the Member States and the Commission may presume that an investment is a direct investment or a FDI.

The first of these is by the Organisation for Economic Co-operation and Development ('OECD'). OECD has developed a benchmark for defining FDIs for the purpose of *inter alia* setting a world standard for direct investment statistics, se the following. According to the OECD, the motivation for the investor in a direct investment is a strategic long-term relationship with the target enterprise to ensure a significant degree of influence over the management of the target company by the investor. This relationship is achieved when the investor owns more than or equal to 10 percent of the voting power of the investment.[61] Moreover, a voting power of 10 percent or more is considered to be evidence that the investor has enough influence to have an effective voice in the management of the investment.[62] Although, the EU is not officially a member of the OECD, OECD policies do have a strong influence on European policies.[63] The Commission has for example stated that 'the extensive analytical work performed by international organisations such as OECD and UNCTAD' lay the basis for a common international investment policy.[64] Moreover, 23 Member States are also

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[60] Council Directive 2013/34/EU of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC [2013] OJ L182/19.
[61] OECD, *OECD Benchmark Definition of Foreign Direct Investment*, 4th edn., 2008, p. 17.
[62] OECD, *OECD Benchmark Definition of Foreign Direct Investment*, p. 50.
[63] European Parliament, S. Mendonca, *The role of the OECD in shaping EU trade policy,* January 2016, [online].
[64] Commission, 'Towards a comprehensive European international investment policy' (Communication) COM (2010) 343 final, p. 4.

members of the OECD.[65] The guidelines may therefore be of guidance for both the Member States and the Commission when determining what investments are FDIs and should thus be taken into consideration by foreign investors investing in the EU.[66]

As previously mentioned, the Commission also considers the analytical work performed by the United Nations Conference on Trade and Development ('UNCTAD') to lay the basis for a common international investment policy. Thus, UNCTADs definition of FDI may also be of guidance for the Member States and the Commission. This essay understands UNCTADs definition of a FDI to be as is explained in the following. The basic difference between FDI and portfolio investments is the intention and expectation of benefits of the investors. Furthermore, FDI is defined as investments made by a resident of one economy in another economy if the investment is of lasting interest or of a long-term nature and if the investor has a significant degree of influence on the management of the target business. A typical FDI is when the investor owns the majority of the voting power or voting shares in a business in another economy, participates in the target business policy-making process and is represented on the board of directors of the target business.[67] Even so, the interest of a direct investment is enabled by a necessary ownership of 10 percent of the voting shares or voting power, however, such a degree of ownership does not necessarily mean that the investment is a direct investment.[68] Instead, FDI are investments made with the intention of a long-term investment of between 10 and 50 percent of the shares of a foreign enterprise as these investments are sufficiently large for the investor to have a role in the management of the target business. Although this ownership of between 10 to 50 percent may not amount to full control over the target business, it is generally sufficient to enable the investor to exercise a significant degree of influence on the management of the target business. In order to confirm that such an investment is a direct investment, the following elements should be considered:

> the members on the board of directors, the composition of the senior executives of the company, the industrial sector of the direct investor and the direct investment enterprise, the names of the companies, technology used by the company, trade between the associate and the

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[65] Austria, Belgium, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Latvia, Lithuania, Luxemburg, Netherlands, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden.

[66] European Parliament, *The role of the OECD in shaping EU trade policy.*

[67] UNCTAD, *FDI Flows and Socks*, (Training Manual on Statistics for FDI and the Operations of TNCs) 1st vol. 2009, p. 38.

[68] UNCTAD, *FDI Flows and Socks*, p. 35.

> direct investor group, loans between the associate and the direct investor and companies related to the direct investor, and trade receivables and trade payables between the same companies.[69]

In summary, UNCTAD states that a direct investment is enabled by a minimum of 10 percent ownership of the voting shares or voting power. However, several other elements must be examined in order to establish if the investment gives rise to a significant degree of influence over the management of the target business.

Another international organization that the EU has a close relationship with is the International Monetary Fund ('IMF'). As the Commission put it in a press release (2020), the EU and IMF are longstanding partners and the partnership 'has intensified over the years with the organizations supporting each other's work'.[70] As the President of the Commission, Ursula von der Leyen, puts it '[t]he European Union and IMF are strong partners'.[71] Thus, IMF's definition of direct investments may be of guidance. IMF has stated that a direct investment enterprise is a company subject to a significant degree of influence or control by a direct investor. Moreover, the IMF stated that such influence or control may be achieved through immediate direct control or indirect direct investment. Here, at least 10 percent holdings of the voting power in the investment by the investor results in an *immediate direct investment relationship*. In such a relationship, control is determined to exist if the investor owns more than 50 percent of the voting power and a significant degree of influence is determined to exist if the investor owns from 10 to 50 percent of the voting power in the investment. Regarding *indirect direct investments relationships*, the IMF has determined them to exist when the ownership of voting power in a direct investment company that owns voting power in another enterprise. Moreover, the IMF recognizes that significant influence or effective control over the investment can arise in less than the above-mentioned percentages of voting power.[72]

To summarize, the definition of direct investments and FDIs by these international organizations seem to indicate that there is a threshold of ownership at around at least 10 percent of the voting power which enables a significant degree of influence or effective control over the target enterprise. However, this does not mean that investors should consider the 10 percent threshold as a general rule. In fact, the case law of the Court clearly indicates

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[69] UNCTAD, *FDI Flows and Socks*, p. 41.

[70] Commission, 'European Commission and International Monetary Fund strengthen cooperation to support sustainable development' (Press release), 28 January 2020, Brussels.

[71] Commission, 'European Commission and International Monetary Fund strengthen cooperation to support sustainable development' (Press release), 28 January 2020, Brussels.

[72] IMF, *Balance of Payments and International Investment Position Manual*, 6th edn., Washington; IMF Multimedia Services Division, 2009, p. 101.

that the ownership of 10 percent of the shares or voting power in another company 'does not necessarily imply that the holder exerts a definite influence over the decisions of the company of which it is a shareholder'.[73] Furthermore, in its working document on FDI in the EU the Commission has explicitly stated that its report does not follow the definition of FDI as 10 percentage of the shares and instead bases FDI on the control of the company.[74] Therefore, investors should be careful not to assume that 10 percent of shares or voting power is a threshold for FDI according to the Regulation. Instead, investors should look at the number as a guideline that indicates that the investment is a direct investment. Furthermore, investors' main concern should always be whether the acquisitions enables effective participation in the control of the target company or a significant degree of influence over the target company.

2.3 Foreign Investor

As previously mentioned, a FDI is an 'investment by a foreign investor'. To understand what investments are subject to the Regulation, we must therefore also understand the term 'foreign investor'. The Regulation defines the term as the following:

> 'foreign investor' means a natural person of a third country or an undertaking of a third country, intending to make or having made a foreign direct investment.[75]

A third country is a state that is not a member of the EU as well as any country or territory whose citizens do not have the use of the right of free movement set forth by Regulation (EU) 2016/399.[76] Thus, natural persons of the EU and companies registered in accordance with the laws of a Member State are not foreign investors. Therefore, a direct investment between an investor in Member State A and a target company or entrepreneur in Member State B is not a foreign direct investment even though the investment has a cross-border context.[77] However, there is an exception to the general rule. The

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[73] Judgement of 3 October 2013, *Itelcar,* C-282/12, EU:C:2013:629, para 22; See also, *Baars,* C-251/98 para 20 and *FII Group Litigation,* C-446/04, para 58.

[74] SWD (2019) 108 final, p. 5; The Commission does not provide an explanation for this choice.

[75] Regulation, art 2(2).

[76] Regulation (EU) 2016/399 of the European Parliament and of the Council of 9 March 2016 on a Union Code on the rules governing the movement of persons across borders (Schengen Borders Code) [2016] OJ L77/1, art 2(5).

[77] TFEU, arts 20(1) and 21; Reg [2016] OJ L77/1, art 2(5).

exception is due to the fact that an investment can originate from a Member State and be directed to a Member State at the same time as the investment contains links to a third country. Thus, we must examine this exception more closely.

2.3.1 Anti-circumvention Clause

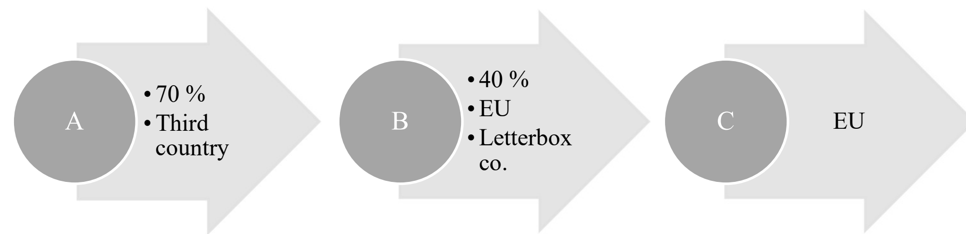
As a general rule, the Regulation enables Member States to screen investments by foreign investors. However, there is an exception. This exception derives from article 3(6) of the Regulation which enables Member States to take measures to identify and prevent circumvention of screening mechanisms or decisions. Such anti-circumvention measures may include the screening of direct investments 'from within the Union by means of artificial arrangements that do not reflect economic reality and circumvent the screening mechanisms and screening decisions'.[78] As the ownership and control of the investor is discussed in section 2.1.1, the following section will not examine these criteria further.

To summarize, there is an exception to the rule that only foreign investors are subject to the Regulation. Therefore, companies residing in the EU, i.e., domestic companies, may also be subject to FDI screening mechanisms.

To clarify the issue, let us examine the following situation. In Figure 1, A, B and C represent different companies. A is registered in a third country whilst B and C are registered in the EU. B is a letterbox company, see more on this below. A is a direct investor in B and owns 70 percent of the shares in B. B then acquires 40 percent of the shares in C which constitutes the largest shareholding in Cs ownership structure. A has control over B, and through this control, A also achieves control over C. Because B is a letterbox company, the direct investment is, *as a general rule,* made through artificial arrangements that do not reflect economic activity to circumvent FDI screening legislation. Therefore, the Regulation enables Member States to screen B's acquisition of the shares in C in accordance with article 3(6) of the Regulation.

[78] Regulation, preamble 10.

Figure 1. Circumvention of national laws



The issue of companies circumventing legislation or reducing regulatory burdens, though establishment in the territory of a Member State in which they do not intend to perform economic activity, is not a new one.[79] Therefore, guidance on when such circumvention is at hand can be found in Community law and in the case law of the CJEU.

According to Wolf Zwartkruis and Professor Bas de Jong with regard to the Regulations anti-circumvention clause, it follows from the case law of the CJEU that restrictions on the freedom of establishment are justified when there is abuse. However, such abuse must be established based on the circumstances of the specific case.[80]

Furthermore, as follows from the case law of the Court, a general principle of Community law is the principle of prohibition of abuse of rights. The Court has also employed the term "circumvention" in case law when referring to similar or identical phenomena as the term 'abuse of rights'. According to advocate General Bobek, in the case of public law where the issue at stake is the scope of application of provisions of Community law and whether these are applied in an 'artificial way', which do not fulfil the legislative purpose of the provisions, the correct terminology for the phenomena of the Principle should be "circumvention".[81] In other words, the opinion of Bobek is that when the Principle is applied in public law, the aim of the principle is not the prohibition of abuse of right but the prohibition of circumvention of legislation.[82]

In conclusion, the principle of prohibition of abuse of rights is applicable when a right is exercised in accordance with the *formal* conditions

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[79] J. Wouters and P. De Man, 'EC Law and Residence of Companies' in G. Maisto (ed.), *Residence of Companies under Tax Treaties and EC law*, Netherlands, 2009, p. 71.

[80] W. Zwartkruis and B. de Jong, 'The EU Regulation on Screening of Foreign Direct Investment: A Game Changer?', *European Business Law Review,* vol. 31, no. 3, 2020, p. 465; Judgement of 30 September 2003, I*nspire Ar,* C-167/01, EU:C:2003:512, para 105.

[81] Opinion of AG Bobek delivered on 7 September 2017, *Edward Cussens, John Jennings, Vincent Kingston v T.G. Brosnan,* C-251/16, EU:C:2017:648, para 23.

[82] This is the interpretation of the author of this thesis; See also opinion of AG Bobek, *Edward Cussens, John Jennings, Vincent Kingston v T.G. Brosnan*, C-251/16, paras 24-25.

established by the law granting said right, but where the legal result of the exercise of the right is against the objective of said law.[83] In other words, the Principle is applicable when the law is formally being followed but the objective of the law is not being upheld.

The principle has previously been applied by the CJEU in relation to Treaty freedoms as well as to other areas of Community law. Scholars Vanessa Edwards and Paul Farmer mention the following situations as examples of when the Court has applied the Principle:

> First, the Court has been confronted on several occasions […] by cases in which nationals of one Member State have used a company incorporated in another Member State as a vehicle to do business in the first Member State with the explicit intention of avoiding certain features of their national company law. Second, ever more sophisticated national legislation designed to target tax avoidance has prompted corporate taxpayers to invoke the freedom of establishment in order to legitimate the arrangements they have put in place wholly or partly with tax considerations in mind.[84]

As the Principle is a general principle of EU law and has previously been applied to the fundamental freedoms of the Union, case law regarding the Principle should be applicable to the free movement of capital. As article 3(6) of the Regulation restricts the free movement of capital for companies registered in the EU, in order to prevent abuse of the free movement of capital in the form of circumvention of national screening mechanisms and screening decisions, the Principle is applicable. Therefore, guidance on when article 3(6) of the Regulation enables Member States to screen direct investments from within the EU can be found in the jurisprudence of the principle of abuse of rights.

In the judgement of *Cadbury Schweppes,* the CJEU discussed the Principle in relation to freedom of establishment with the following conclusion. Nationals of a Member State may not use the possibilities granted to them by the TFEU to circumvent national legislation. In other words, they may not abuse the provisions established by Community law.[85] However, the fact that a company is established in a Member State for the purpose of benefiting from legislation in said Member State is not an abuse of the

[83] A. Lenaerts, 'The General Principle of the Prohibition of Abuse of Rights: A Critical Position on Its Role in a Codified European Contract Law'*, European Review of Private Law,* vol. 18, no. 6, 2010, pp. 1121-1122.
[84] V. Edwards and P Farmer, 'The Concept of Abuse in the Freedom of Establishment of Companies: a Case of Double Standards?' in A. Arnull, P. Eeckhout, and T. Tridimas (eds.), *Continuity and Change in EU Law: Essays in Honour of Sir Francis Jacobs*. Oxford University Press; 2008, p. 208.
[85] Judgement of 12 September 2016, *Cadbury Schweppes*, C-196/04, EU:C:2006:544, para 35.

provisions established in Community law. Furthermore, the Court has stated that when a restriction is to be justified on the ground of prevention of abusive practices, ‘the specific objective of such a restriction must be to prevent conduct involving the creation of wholly artificial arrangements which do not reflect economic reality’.[86] Let us stop here for a second and recall that the Regulation enables Member States to screen direct investments by companies registered in a Member States if the investments is by means of ‘artificial arrangements that do not reflect economic reality’.[87] With that in mind, let us return to examining the case law of the Court.

According to the Court, the concept of wholly *artificial arrangements which do not reflect economic reality*, involves (1) a subjective element of the intention to obtain an advantage, and (2) objective circumstances demonstrating that the objective pursued by the freedom has not been achieved despite formal observance of the conditions laid out.[88] Moreover, an entity has characteristics of wholly artificial arrangements, if the entity is a fictitious establishment which does not carry ‘out any genuine economic activity in the territory of the host Member State’.[89] When determining if the entity intends to carry out genuine economic activity in the host Member State, objective factors which are ascertainable by third parties should be considered, in particular, to what extent the entity exist in terms of staff, premises and equipment.[90] Moreover, if the checking of these factors leads to the conclusion that the company in question is a letterbox or front subsidiary, the creation of said company should, in particular, be regarded as having characteristics of a wholly artificial arrangement.[91] In the judgement of *Eurofood IFSC* the Court determined that ‘letterbox’ companies are those which do not carry out any business in the territory of the Member State in which its registered office is situated.[92]

Correspondingly, in the Judgement of *Halifax and Others* the Court stated that the Principle of prohibition of abuse is not relevant where the economic activity that is carried out by the enterprise may have another explanation than attaining advantages. Therefore, it must be apparent from objective factors that the main objective of the concerned transaction is to obtain an advantage.[93]

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[86] *Cadbury Schweppes*, para 55.
[87] Regulation, preamble 10.
[88] *Cadbury Schweppes*, para 64.
[89] *Cadbury Schweppes*, para 68.
[90] *Cadbury Schweppes,* para 67.
[91] *Cadbury Schweppes,* para 68.
[92] Judgement of 2 May 2006, *Eurofood IFSC,* C-341/04, EU:C:2006:281, para 34.
[93] Judgement of 21 February 2006, *Halifax and Others*, C-255/02, EU:C:2006:121, para 75.

Of interest in the question of circumvention of national legislation is also the Courts statement in the *Part Service* case. The companies involved in the case had divided contracts regarding the leasing of vehicles into separate parts. The Court stated that, separate transactions should be assessed together where 'if in the course of a purely objective analysis, it is found that there is a single supply'.[94] It is therefore legitimate to question whether this means that the following is maybe true: If a foreign investor transfers capital to a national of a Member State and this person, legal or natural, then uses said capital to make a direct investment, these separate transactions should be assessed together and because of this, the investment by the national of a Member State should be subject to FDI screening mechanisms. This question however has not been examined in the literature, but this thesis argues that there is room for these separate transactions to be interpreted as a single transaction in the context of FDI screening mechanisms.

In conclusion, the case law regarding the Principle indicates that 'investments from within the Union by means of artificial arrangements which do not reflect economic reality and circumvent the screening mechanisms and screening decisions',[95] are investments where (1) the foreign investor intents to obtain an advantage by making a direct investment through a subsidiary or otherwise owned and controlled entity established in a Member State instead of making the direct investment themselves if, (2) said entity does not carry out genuine economic activities with regards to employees, premises and equipment, and in particular if the entity does not perform any business in the territory of the Member State in which its registered office is situated.

To summarizes, the right of free movement of capital can be restricted on the grounds of public policy or public security. The Regulation enables Member States to screen direct investments into their territory by companies registered in the Union if certain conditions are met in order to hinder abuse of the free movement of capital. The case law of the CJEU regarding the principle of prohibition of abuse of rights may be of guidance in determining when such restrictions on the free movement of capital and the freedom of establishment are justified. In conclusion, it may not be possible for foreign investors to circumvent the Regulation by having a subsidiary, registered in the Union, perform direct investments on behalf of the foreign investor.

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[94] Judgement the Second Chamber of the Court of 21 February 2008, *Ministero dell'Economia e delle Finanze v Part Service Srl*, C-425/06, para 52; Opinion of AG Bobek delivered on 7 September 2017, *Edward Cussens and Others v T.G. Brosnan*, C-251/16, ECLI:EU:C:2017:648, para 68.

[95] Regulation, preamble 10.

2.3.2 Special-Purpose Entities

As follows from the case law of the CJEU, if a company does not perform any genuine economic activity in the territory of the host Member State, said company has characteristics of wholly artificial arrangements.[96] When such a company is owned or controlled by a foreign investor and the investment does not reflect the economic reality, the investment may have been performed by said company with the intent of circumventing national screening mechanisms. The description of such a company[97] does, in the opinion of this thesis seem eerily similar to the definition of Special-Purpose Entities ('SPE'). Therefore, this thesis suggests that guidance on what entities established in the EU risk having their direct investments screened may be found in the definition of SPEs. The definition of SPEs is the following:

> An SPE, resident in an economy, is a formally registered and/or incorporated legal entity recognized as an institutional unit, with no or little employment up to maximum of five employees, no or little physical presence and no or little physical production in the host economy.
>
> SPEs are directly or indirectly controlled by nonresidents.
>
> SPEs are established to obtain specific advantages provided by the host jurisdiction with an objective to (i) grant its owner(s) access to capital markets or sophisticated financial services; and/or (ii) isolate owner(s) from financial risks; and/or (iii) reduce regulatory and tax burden; and/or (iv) safeguard confidentiality of their transactions and owner(s).
>
> SPEs transact almost entirely with nonresidents and a large part of their financial balance sheet typically consists of cross-border claims and liabilities.[98]

Let us examine the following example concerning a SPE. The company *Invest AB* is registered in Sweden, it has one employee, no physical presence except for a post-box and no physical production in Sweden. The Company *Invest Colombia AB* which is registered in Colombia owns 70 percent of the shares in Invest AB. Invest Colombia AB established Invest AB in Sweden to gain access to the capital markets of the EU, reduce the regulatory burden of FDI screening mechanisms and to safeguard the confidentiality of their transactions. Based on these characteristics, the company Invest AB matches

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[96] *Cadbury Schweppes*, para 68

[97] I.e. a company that is owned or controlled by a foreign national and which does not intent to carry out genuine economic activity or, as is the case with letterbox companies, any economic activity at all.

[98] Statistics Department IMF, 'Final Report of the Task Force on Special Purpose Entities', Washington D.C., IMF, 2018, p. 6, [online].

the definition of a SPE. Once Invest AB has been established in Sweden, Invest Colombia AB transfers assets to Invest AB which Invest AB then uses to acquire 40 percent of the shares in the Danish start-up 'AI AB', which specialises in artificial intelligence.

Is the example above an investment (1) by means of artificial arrangements that do not reflect economic reality, which (2) circumvent the screening mechanism and screening decisions and, (3) where the investor is ultimately owned or controlled by third-country national?[99] To begin with, Invest AB does not perform economic activity in Sweden, thus, according to the case law of the Court, Invest AB has characteristics of wholly artificial arrangements.[100] Secondly, as Invest AB only has one employee, a post-box and no actual equipment in Sweden or in any other Member State, there are indicators that Invest AB does not intent to carry out any genuine economic activity in Sweden.[101] Based on the examined factors, the example of Invest AB is an investment which can be subject to FDI screening mechanisms under article 3(6) of the Regulation. Even so, one must remember that the Member States can choose not to screen a direct investment even when the investment can be subject to national screening mechanisms and screening decisions.[102] The Member States may, for instance, choose not to screen certain FDI in order to attract foreign investors or to be a more competitive destination for FDI.

To summarize, this thesis suggests that guidance on what direct investments by companies registered in the EU can be subject to screening mechanisms and screening decisions can be found in the definition of SPEs. Therefore, foreign investors who wish to perform direct investments in the EU through subsidiaries established in the EU should consider whether their subsidiary is a SPE before performing any direct investments through said subsidiary if the intention of such a transaction is to circumvent national screening mechanisms or screening decisions.

2.4 Preliminary Analysis

Foreign direct investments are direct investments and direct investments are capital movements. Capital movements to and from the Member States are protected against restrictions by the free movement of capital. However, Member States can take measures to restrict the free movement of capital on the grounds of public security or public order.

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[99] Regulation, art 3(6) and preamble 10.

[100] *Cadbury Schweppes*, para 68.

[101] *Cadbury Schweppes*, paras 66-68.

[102] Regulation, art 1(3).

Foreign direct investments are those which serve to establish or maintain lasting and direct links between the investor and the target company, or the entrepreneur to whom the capital is made available, in order to carry out economic activity. Such links are established when the investor has the possibility of participating effectively in the management of a company or in its control. The investor has objectively achieved effective control over the target company's economic activities when the investors consent is needed, alone or with others, to carry out important or major entrepreneurial decisions. Such control can be achieved through the acquisition of shares or voting power in the target company. Furthermore, the investor is effectively participating in the management of the target company when he or she takes an active part in everyday tasks of administrative, executive, and supervisory direction.

Although there is no certain threshold at which effective control over the target company is achieved, there are indicators of such a threshold in secondary sources of law and in the work of international organisations. These sources indicate that an acquisition of at least 10 percent of the voting power generally enables control of an investment. However, the CJEU has established that the holding of 10 percent of shares or voting rights in a company does not necessarily enable the holder definite influence over the company's decisions. Therefore, other elements must be examined in order to determine if such is the case, for example if the holder is participating in the everyday management of the company. Moreover, the following elements may, amongst others, be of guidance: the members on the board of directors in the target company, the industrial sectors of the investor and the target company and the names of the investor and the company.

Foreign direct investments must, as a principal rule, be made by foreign investors, that is to say, a natural person or a company of a third country. A natural person of a third country is located where they normally stay, and a company of a third country is located in the state to which it shows a continuous and effective link to the economy of said state. With that said, the Regulation also enables Member States to screen direct investments from within the EU if the investor is ultimately owned or controlled by a natural person or undertaking of a third country if the investment is made by means of artificial arrangements that do not reflect economic reality and circumvent national screening mechanisms and screening decisions.

When determining if a such circumvention of national screening mechanisms or screening decisions is at hand, the case law of the Court regarding the principle of prohibition of abuse of rights can be of guidance. The Principle applies when the formal criteria of a law granting a right is being upheld but the legal result of the exercise of the right is against the objective of the law granting it. The objective of the free movement of capital is to remove restrictions on the movement of capital, unless certain exceptions

are at hand. Thus, if the investment is such that it may fall within the exceptions, as in, if the investment can threaten the public order or public security of the Member State, the objective of the freedom is not upheld. In other words, if the direct investment from within the EU can threaten public order or public security, the investment does not fulfil the objective of the free movement of capital. Therefore, the Principle of abuse of rights is applicable to such investments.

When determining if a practice constitutes abuse, the circumstances in the individual case must be examined. As follows from the case law of the Court regarding the abuse of rights, direct investments from within the EU are made by means of artificial arrangements that do not reflect economic reality if the following is true: the intention behind the investment is to obtain an advantage and the objective of the free movement of capital has not been achieved. Furthermore, if the direct investor from within the EU is a company that does not carry out any genuine economic activity in the territory of the host Member State, the company has characteristics of artificial arrangement which do not reflect economic reality. When determining if the company carries out economic activity, factors such as staff, premises and equipment should be examined.

Furthermore, this thesis suggests that when examining if a company, making direct investments from within the EU, is by means of artificial arrangements that do not reflect economic reality and circumvent the screening mechanisms and screening decisions, the definition of special-purpose entities can be of guidance. In other words, it is the opinion of this thesis that special-purpose entities, generally, involve the creation of wholly artificial arrangements which do not reflect economic reality and that therefore, investments by such companies can, generally, be screened under article 3(6) of the Regulation. Thus, when examining if a direct investment from within the EU by a company can be screened under article 3(6) of the Regulation, the company's characteristics should be compared to those that define special-purpose entities.

This thesis also suggests that in a situation where capital has been transferred from a foreign investor to a company registered in a Member State, and that same capital is then used by said company to perform a direct investment from within the Union, the transfer of the capital and the direct investments may be considered as one transaction, thus making the investment a foreign direct investment. With that said, it is important to note that this suggestion derives from application of case law of the Court and has not been examined by literature.

3 Challenges For Foreign Investors

As the previous chapter examined what investments were subject to the Regulation, this chapter will examine the Regulation and what challenges it may present for foreign investors.

3.1 About the Regulation

To begin with, let us examine some of the basic aspects of the Regulation. When the Regulation mentions *screening*, it refers to a procedure which allows the Member States to 'assess, investigate, authorise, condition, prohibit or unwind foreign direct investments'.[103] In the same way, the term *screening mechanisms* refers to an instrument or general application which accompanies administrative requirements and implements guidelines or rules which set the procedures, conditions or terms to 'assess, investigate, authorise, condition, prohibit or unwind foreign direct investments on grounds of security or public order'.[104] Furthermore, when the Regulation refers to *foreign direct investment undergoing screening*, it refers to a foreign direct investment being formally assessed or investigated in a manner compatible with screening mechanisms.[105]

The Regulation enables Member States to maintain, adopt or amend screening mechanisms in their territory on the grounds of public order or security.[106] Thus, the Regulation does not restrict capital movements in itself, instead it enables the Member States to restrict capital movements by screening mechanisms and screening decisions. The rules and procedures regarding screening mechanisms implement by the Member States pursuant to the Regulation are to be transparent and non-discriminatory. Furthermore, when applying timeframes for screening mechanisms the Member State shall take into account the timeframes for comments from other Member States and opinions from the Commission, as further explained in section 3.4.[107]

As previously mentioned, a Member State that has implemented screening mechanisms can undertake screening of FDI into their territory on grounds of public order or security.[108] When determining if a FDI is likely to

[103] Regulation, art 2(3).
[104] Regulation, art 2(4).
[105] Regulation, art 2(5).
[106] Regulation, art 3(1).
[107] Regulation, art 3(3).
[108] Regulation, art 1.

affect the aforementioned grounds, the Member States can find guidance in article 4 of the Regulation.

3.2 Factors of Interest

Article 4 of the Regulation contains the following non-exhaustive list of factors the Member States may consider when determining if a FDI is 'likely to affect security or public order':[109]

> (a) critical infrastructure, whether physical or virtual, including energy, transport, water, health, communications, media, data processing or storage, aerospace, defence, electoral or financial infrastructure, and sensitive facilities, as well as land and real estate crucial for the use of such infrastructure;
>
> (b) critical technologies and dual use items as defined in point 1 of Article 2 of Council Regulation (EC) No 428/2009 (15), including artificial intelligence, robotics, semiconductors, cybersecurity, aerospace, defence, energy storage, quantum and nuclear technologies as well as nanotechnologies and biotechnologies;
>
> (c) supply of critical inputs, including energy or raw materials, as well as food security;
>
> (d) access to sensitive information, including personal data, or the ability to control such information; or
>
> (e) the freedom and pluralism of the media.[110]

The article also mentions the following factors which the Member States and Commission may take into account, in particular, when determining if a FDI is likely to affect security or public order:

> (a) whether the foreign investor is directly or indirectly controlled by the government, including state bodies or armed forces, of a third country, including through ownership structure or significant funding;
>
> (b) whether the foreign investor has already been involved in activities affecting security or public order in a Member State; or
>
> (c) whether there is a serious risk that the foreign investor engages in illegal or criminal activities.[111]

Furthermore, the Commission has stated that Member States, when examining FDI into companies whose true value is higher than its valuation

[109] Regulation, art 4(1-2).
[110] Regulation, art 4(1).
[111] Regulation, art 4(2).

on capital markets, should take into account the *potential impact* of the investment on public policy or security. For example, if the investment may result in over-dependency on that foreign investor for the supply of essential goods.[112]

The intent of article 4 of the Regulation is to provide guidance as to what factors may be of import in the determination of how a FDI may affect security or public order. Moreover, article 4 is also intended to improve transparency for foreign investors considering investing in the EU. Nonetheless, the Member States are free to consider other factors based on their national needs and the decision of what factors actually are of import is left to the Member States.[113] With that in mind, even if that Member State finds that a FDI is likely to affect security or public order based on the factors mentioned in article 4, they cannot based on this alone decide to prohibit, condition or unwind the investment. The reason being that article 4 does not constitute a threshold for government intervention. This is because restrictions on the free movement of capital per the Regulation are permitted based on the grounds of public security and public policy as per article 65 TFEU.[114] From the jurisprudence of the Court follows that restriction on fundamental freedoms can only be justified on grounds of public policy or public security if 'there is a genuine and sufficiently serious threat to a fundamental interest of society'.[115] Therefore, while article 4 is of import for the determination if the FDI is likely to affect security or public order, the Member States cannot prohibit a FDI solely based on the fact that it is *likely* to affect public order or security.

Furthermore, the Member State are not obligated to publish the principles guiding their decision. This is unfortunate as such published work would be of future guidance for foreign investors wanting to invest in said Member State.[116]

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[112] C (2020) 1981 final, p. 5.
[113] S. Hindelang and A. Moberg, 'The art of casting political dissent in law: The EU'S framework for the screening of foreign direct investment', *Common Market Law Review,* vol. 57, no. 5, 2020, pp. 1448-1449; Regulation, art 4 and preamble 8 and 12.
[114] COM (2017) 487 final, p. 4.
[115] *Église de Scientologie,* para 17.
[116] S. Hindelang and A. Moberg, 'The art of casting political dissent in law', p. 1447.

3.3 Public Security and Public Order

As mentioned in the previous section, Member States may impose restrictions on FDI into the EU on grounds of security or public order.[117] Thus, it becomes necessary to examine what constitutes as grounds of security or public order.

To begin with, the national security of a Member State is the sole responsibility of said Member State.[118] Accordingly, the Member States enjoy discretion in determining the requirements of public policy and public security based on their national needs.[119] Yet, this does not mean that Member States can unilaterally determine the public interests without any control by the institutions of the Union. Instead, restrictions based on these public interests must be proportional, comply with the general principles of EU law, such as the principle of legal certainty, and must not be implemented due to wholly economic ends.[120] Furthermore, the relied upon public interest must be interpreted strictly and may not be relied upon unless there is a genuine and sufficiently serious threat to a fundamental interest of society.[121] Moreover, the Court stated restrictions on the free movement of capital can only be justified on grounds of public security or public order if the measures are 'necessary for the protection of the interests which they are intended to guarantee and only in so far as those objectives cannot be attained by less restrictive measures'.[122] Furthermore, such measures must not 'constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital'.[123] The purpose thereof is to ensure that the Member States do not exercise this right in order to achieve discriminatory purposes.[124]

With that said, the case law of the Court states that movements of capital to and from third countries 'takes place in a different legal context from that which occurs within the Community'.[125] Thus, it is possible that Member

[117] Regulation, arts 1(1) and 3(1).

[118] Consolidated version of the Treaty on European Union [2012] OJ C326/13, art 4(2).

[119] Judgement of 9 December 1997, *Strawberries,* C-265/95, EU:C:1997:595, para 33; COM (2017) 487 final, p. 4.

[120] Judgement of 13 May 2003, *Commission v. Kingdom of Spain,* C-463/00, EU:C:2003:272, para 34.

[121] Judgement of 8 November 2012, *Commission v. Hellenic Republic*, C-244/11, EU:C:2012:694, para 67; COM (2017) 487 final, p. 4.

[122] *Église de Scientologie,* para 18.

[123] TFEU, art 65(3).

[124] D. Bugge Thorbjørn, 'Comment on "In Search for an EU Competence to Establish an Investment Screening Mechanism and Restricting Effects Flowing from Fundamental Freedoms, Fundamental Rights, and Other EU Primary Law"', in S. Hindelang and A. Moberg (eds.), *YSEC Yearbook of Socio-Economic Constitutions 2020,* Springer Nature Switzerland AG, 2020, p. 7.

[125] Judgement of 18 December 2007, *Skatteverket*, C-101/05, EU:C:2007:804, para 36.

States will be able to justify restrictions on the free movement of capital between Member States and third countries more broadly than between Member States.[126]

As follows from EU law, the Member States have a measure of freedom when establishing what constitutes a threat against security or public order. This notion is supported by the Commission which has stated that the Regulation should provide the necessary flexibility for Member States to consider their national circumstances and individual situation when screening FDIs on grounds of security or public order.[127] From this follows that EU law does not contain a definition of what constitutes grounds of security or public policy.

Furthermore, in the context of FDI as M&A deals, there is yet another aspect of public policy or security to consider. When a M&A deal constitutes a concentration which falls within the scope of Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (Merger Regulation),[128] then the grounds for screening and the notion of legitimate interests in article 21(4) of the Merger Regulation should be interpreted in a coherent manner.[129] Thus, guidance on what constitutes grounds of public policy and security may be found in the case law of the CJEU and decisions from the Commission regarding merger control proceedings. With that said, it is important to remember that while the Merger Regulation contains thresholds for what concentrations can be investigated, the Regulation does not contain any such thresholds. This means that not all concentrations that are screened based on the Regulation falls within the scope of the Merger Regulation. Therefore, it is important to note that the grounds of screening and the legitimate interests of the Merger Regulation should only be interpreted in a coherent manner when concentrations fall within the scope of both Regulation. With that said, let us examine the CJEU interpretation of 'legitimate interests' in the context of the Merger Regulation. First off, the Merger Regulation identifies three categories of legitimate interests (1) plurality of the media, (2) public security and (3) prudential rules. Furthermore, the Commission can recognize additional public interests by an *ex ante* review.[130] The concept of public security in accordance with merger control can for example be relied upon in regards to the security of supplies of a service or product or essential or vital interest for the safeguarding of

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[126] *FII Group Litigation*, para 171.
[127] COM (2017) 487 final, p. 17.
[128] Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings [2004] OJ L24/1.
[129] Regulation, preamble 36.
[130] Merger Regulation, art 21(4).

public health.[131] Similarly, it is clear from both the Regulation and the communication from the Commission regarding FDI screening mechanisms that security or public order can be relied upon in order to protect health infrastructure and supply.[132]

When determining if a measure is justified based on public policy or security Member States may consider their national needs. Yet, the measures must be proportional, comply with the general principles of EU law and must not discriminate. Furthermore, public policy or security can only be relied upon if there is a genuine and sufficiently serious threat to a fundamental interest of society. When the FDI in question constitutes an M&A deal, guidance on what constitutes a threat against public order or security may be found in the case law of the Court regarding merger control.

3.4 Foreign Investors Controlled by the State

According to the joint letter sent to the Commissioner, a key point for Germany, France and Italy in proposing investment reviews at EU level was the ability to intervene against state-funded takeovers which were based on political programs.[133] Accordingly, in 2017, the Commission recognized that there existed 'concerns about foreign investors, notably state-owned enterprises, taking over European companies with key technologies for strategic reasons',[134] and that these concerns needed 'careful analysis and appropriate action'.[135] Furthermore, as follows from the Commissions 'white paper on levelling the playing field as regards foreign subsidies' (2020), the Commission takes any potential distortion on competition in the internal market by foreign capital seriously. In the white paper, the Commission states that new legislation of foreign subsidies would be complementary to the Regulation.[136] However, such legislation does not exist yet and the current provision in EU competition policy does not provide an appropriate way to

[131] Directorate for financial and enterprise affairs competition committee, 'Public interest considerations in merger control', OECD, 2016, p. 4 [online].
[132] Regulation, art 4(1)(a); C (2020) 1981 final, p. 1-2.
[133] B. Zypries, M. Sapin and C. Calenda, 'Proposals for ensuring an improved level playing field in trade and investment' [letter to Commissioner C. Malmström], February 2017; Commission, 'EU-China – A strategic outlook' (Joint communication) JOIN (2019) 5 final, p. 8.
[134] Commission, 'Reflection paper on harnessing globalization' COM (2017) 240 of 10 May 2017, p. 15.
[135] COM (2017) 487 final, p. 1.
[136] Commission, 'White paper on levelling the playing field as regards foreign subsidies' COM (2020) 253 final, p. 43.

deal with the issues posed by foreign capital in the EU, for instance through third country's state financing of foreign enterprises in the Union.[137]

Thus, it is hardly surprising that Member States are encouraged to take into account, in particular, if the foreign investor is owned or controlled by the government of a third country when determining if an investment is likely to affect public order or security.[138] At first glance, this provision may not alarm foreign investors. However, the provision may well lead to unexpected consequences due to the relationship between EU investment law and EU competition law.

As previously discussed, M&A deals can in some circumstances be subject to FDI screening mechanisms. However, M&A deals can also be challenged by the Commission or by the Member States on the basis of competition law. Thus, M&A deals can be challenged by both competition law and investment law in the EU on different grounds. In the context of state-ownership, there is one difference between the two Regulations that may be of interest. While the Merger Regulation does permit the Commission and the Member States to challenge concentrations based on legitimate interests, as discussed previously, the Merger Regulation does not permit discrimination based on the ownership of the acquirer, i.e. the investor. Thus, the ownership status of the foreign investor cannot justify restrictions on a concentration on the basis of the Merger Regulation. Scholars have long argued that the inability to consider the ownership status of the acquirer into consideration is a flaw of the Merger Regulation. The Regulation, on the other hand, encourages Member States to take the ownership structure of the foreign investor into account.[139]

In summary, the competitive disturbances that state-ownership of foreign investors can cause, have long been a topic of concern in the EU. At the moment, there exist no appropriate legislation to deal with this issue even if one may be on the way. Therefore, it is not impossible that Member States will make use of the Regulation to handle the issue until such a time where another legislation enters into force. Because of this, the factor of state-control may be the factor of most import for both the Member States and foreign investors. Thus, the concept of state-control must be examined more closely.

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[137] JOIN (2019) 5 final, p. 8.

[138] Regulation, art 4(2)(a).

[139] G. Pandey, D. Rovetta and A. Smiatacz, 'How Many Barriers Should a Steeple Chase Have? Will the EU's Proposed Regulation on Screening of Foreign Direct Investments Add yet More Delaying Barriers When Getting a Merger Deal through the C', *Global Trade and Customs Journal*, vol. 14, no. 2, 2019, p. 59; B. Zypries, M. Sapin and C. Calenda, 'Proposals for ensuring an improved level playing field in trade and investment' [letter to Commissioner C. Malmström], February 2017.

3.4.1 State-Control

From article 4 of the Regulation follows that Member States should take into account, in particular, if a foreign investor is controlled by the government of a third country. The control can be both indirect and direct and includes control through significant funding and ownership structure. Thus, we know that the concept of state-control includes control through ownership structure or in other words, state-ownership. Therefore, we must examine the concept of state-owned enterprises ('SOEs'). There is no internationally recognized definition of SOEs. With that said, the Commission has previously defined SOEs as 'all those non-financial companies where the state exercises control, regardless of the size of ownership'.[140] The Commission has stated that SOEs especially include the following three categories:

1. enterprises whose shares are fully owned by public authorities,
2. enterprises in which public authorities have majority shareholdings, and
3. enterprises in which public authorities have minority shareholdings together with special powers given by statute law.[141]

Additionally, the Commission mentions that enterprises in which public authorities have a minority shareholding and no special powers are relevant for assessing governments' stakes in the economy. Therefore, we cannot rule out that this last category may be of import for the interpretation of state-controlled enterprises even if the enterprises are not state-owned.[142]

To summarize, SOEs are those over which the state exercises control regardless of the size of the state's ownership. In cases where the foreign investor is owned, at least partly, by the Government of a third state, guidance on state-control can be found in the definition of state-owned enterprises. Furthermore, the Commission has had reason to examine state-control over state-owned enterprises previously in the context of turnover of enterprises owned by the state in merger control proceedings. The Commission has for example stated that a SOE should be treated as independent from other SOEs in the context of turnover when it is not under any coordination with other

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[140] Commission, 'State-Owned Enterprises in the EU: Lessons Learnt and Ways Forward in a Post-Crisis Context' (Institutional paper 031), July 2016, p. 6 [online].
[141] Commission, Commission, 'State-Owned Enterprises in the EU: Lessons Learnt and Ways Forward in a Post-Crisis Context', pp. 6-7.
[142] COM (2017) 487 final, p. 17.

SOEs.[143] Therefore, the Commission has had reason to examine when state-owned enterprises operate independently from one another. Thus, the criteria which the Commission have used to determine when state-owned enterprises are subject to state-control may be of guidance in the determination of state-control in the context of FDI.

In the context of state-control in merger control proceedings, the Commission has for example stated that two or more SOEs which have power of decision independent from one another and independent from the State are not considered to be under the same controlling entity and vice versa. From this one can draw the conclusion that where the power of decision in the company lays may be of import in the determination of state-control. Furthermore, the Commission has identified, *inter alia*, the following elements as factors of value when determining if SEOs have independent decision making power from each other: the States' possible power to influence the entities commercial strategy, the interlocking directorship between entities owned by the same entity and the likelihood for the State to coordinate their commercial conduct.[144] Thus, these elements may be of value for determining whether a SOE is under the state-control or not.

Regarding control by the government through significant funding, please see section 4.3 to learn more about how control can be achieved in this way.

To summarize, the Regulation encourages Member States to take into account, in particular, if the foreign investor is under the control of the government of a third country. Such control can be the result of, for example, shareholdings by public authorities or significant funding. When determining if a company is under state-control and said company is at least partly owned by the State, guidance can be found in the Commission's definition of state-owned enterprises.

3.5 Opinions, Comments and Information Requests

If a Member State decides to screen a FDI in their territory, the Member State must notify the other Member States and the Commission as soon as possible. If any of the other Member States believes that said investment is likely to

[143] Commission, 'Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings' [2008] OJ C95/1, para 194.
[144] China National Bluestar/Elkem (Case COMP/M.6082) Commissions Decision [2011] C (2011) 2429 final, p. 10.

affect its security or public order, or if they have relevant information, they can provide comments to the Member State in which territory the FDI is taking place. Such comments are also sent to the Commission.[145] Furthermore, the same applies to the Commission. If the Commission believes that a FDI undergoing screening in a Member State is likely to affect security or public interests in two or more Member States or have relevant information on the matter, the Commission can issue an opinion addressed to the Member State in which the FDI is being screened. The Commissions may issue an opinion following comments from the Member States or independently from such comments. If at least a third of the Member States believe that a FDI is likely to affect security or public order, the Commission must issue such an opinion, if justified.[146] After having received notice from the screening Member State, the other Member States and the Commission have 15 days (as in calendar days) to notify the screening Member State if they intend to perform such measures, and while doing so they can also request additional information. Furthermore, they must perform such measures no later than 35 days following the notification from the Member State undertaking screening or no later than 20 calendar days after having received additional information. Moreover, following comments from other Member States, the Commission may issue an opinion up to five calendar days after the deadlines mentioned.[147]

Even if the Member State in which the FDI is taking place does not screen a FDI that is planned or completed in its territory, the other Member States can provide comments and the Commission can issue an opinion on the FDI if it is likely to affect security or public order or if they have relevant information and it is duly justified. In this case, they may also request necessary, proportionate and not unduly burdensome information from the Member State in which territory the FDI is or has taken place.[148] Such comments or opinions shall be issued no later than 35 days following the obtainment of the requested information.[149] In cases where the Commission's opinion follows comments, the Commission has an extra 15 days to issue an opinion. Furthermore, if the FDI has already been completed without screening then the Member States and the Commission may provide comments and issue opinions up to 15 months after the FDI has been completed.[150] As explained by the Commission in its communication to the Member States, such comments and opinions within the 15-month period may

[145] Regulation, art 6(1-2).
[146] Regulation, art 6(3).
[147] Regulation, art 6(6-7) (with some exceptions).
[148] Regulation, art 7(5).
[149] With some exceptions, see Regulation, arts 7(6) and 9(5).
[150] Regulation, art 7(8).

lead Member States to adopt measures, including mitigating measures such as supply commitments.[151]

The Member State in which the investment is taking place or has taken place shall give due consideration to the comments by the other Member States and the opinions of the Commission. However, the decision to screen an investment shall always be taken by the Member State in which the screening would take place.[152] When appropriate, the territory Member State, shall take measures available under its national law or in its broader policy-making in order to cooperate with the issued comments or opinion.[153]

Additionally, the Commission may provide an opinion when a FDI is likely to affect projects and programmes of Union interests.[154] The territory Member State shall take *utmost account* of this opinion through, where appropriate, measures available under its broader policy-making or national laws. Moreover, if the Member State do not follow the opinion, they must provide an explanation to the Commission.[155]

All opinions issued by the Commission lack binding force.[156] However, the fact that the opinions lack binding force may not necessarily mean that they cannot affect the investment.[157] Lawyers Giani Pandey and Davide Rovetta as well as senior EU and Trade legal Researcher Agnieszka Smiatacz argue that the non-binding nature of Opinions by the Commission are to the disadvantage of would-be investors. According to them, the national authorities of Member States are likely to feel obligated to follow the Commissions Opinions even though they are non-binding. Furthermore, they argue that the jurisprudence of the CJEU regarding the term *utmost account* signifies that the Member States, *de jure*, will be subject 'to a higher standard to be able to deviate from the Commission's Opinion' regarding investments which are likely to affect projects or programmes of Union interest.[158] The term utmost account has been examined by the Court in the judgment of *Koninklijke KPN NV and Others*:

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[151] C (2020) 1981 final, p. 4; See also Commission, 'Coronavirus: Commission issues guidelines to protect critical European assets and technology in current crisis' (Press release), 25 March 2020, Brussels.
[152] Regulation, arts 6(9) and 7(7).
[153] Regulation, preamble 17.
[154] Regulation, art 8; See also Annex to the Regulation for projects and programmes of Union interest.
[155] Regulation, preamble 19.
[156] TFEU, art 288.
[157] T. M. Hagemeyer, 'Access to Legal Redress in an EU Investment Screening Mechanism', in S. Hindelang and A. Moberg (eds.), *YSEC Yearbook of Socio-Economic Constitutions 2020*, Springer Nature Switzerland AG, 2020, pp. 12-12.
[158] Pandey, Rovetta and Smiatacz, '*How Many Barriers Should a Steeple Chase Have?*, p. 59.

> Nevertheless, the second subparagraph […] requires NRAs, in carrying out their duties, to 'take the utmost account' of the Commission recommendations.
>
> Accordingly, it is for the NRA, […], to follow, as a rule, the guidance contained in Recommendation 2009/396. It is only where it appears to the NRA, in its assessment of a given situation, that the […] advocated by this recommendation is not appropriate to the circumstances that it may depart from it, giving reasons for its position.[159]

Thus, the jurisprudence of the Court suggests that the term signifies that the national authorities of Member State, as a rule, are to follow the Commission's Opinions when programs or projects of Union interest are likely to be affected, with one exception. The exception being when the Opinion is not appropriate to the circumstances in a given situation.

Additionally, Judge Hagemeyer suggests that, although comments and opinions lack binding force, they may cause investment deals to fall through due to the threat of regulatory encroachment.[160] Furthermore, Hagemeyer argues that even though Opinions by the Commission may very well affect the screening decision by the national authorities of the Member State in which screening is taking place, investors cannot achieve recourse against an opinion by the Commission.[161] See more on recourse in the next section.

3.6 Recourse

Foreign investors whose investments into the EU have been conditioned or prohibited may feel that the national authority's screening decision is wrong and, for example, that the FDI does not in fact constitute a genuine and sufficiently serious threat against public policy or security. Or perhaps nationals of a Member State whose investment has been screened based on article 3(6) may believe that their investment does not fulfil the requirements of screening under article 3(6) of the Regulation. For these unsatisfied investors, the Regulation offers the possibility to seek recourse against the Member States screening decisions:

> Foreign investors and the undertakings concerned shall have the possibility to seek recourse against screening decisions of the national authorities.[162]

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[159] Judgement of 15 September 2016, *Koninklijke KPN NV and Others,* C-28/15, EU:C:2016:692, paras 37-38.

[160] Hagemeyer, *Access to Legal Redress in an EU Investment Screening Mechanism*, p. 9.

[161] Hagemeyer, *Access to Legal Redress in an EU Investment Screening Mechanism,* p. 13.

[162] Regulation, art 3(5).

As follows from the article, recourse if not defined in the Regulation. Therefore, other sources must be examined in order to understand the recourse available to investors.

First of all, it follows from the principle of procedural autonomy that, in the absence of Community rules, the legal system of each Member State must designate the courts having jurisdiction and 'establish procedural rules for actions intended to safeguard the rights of individuals'.[163] However, if the situation is governed by EU law, the principle of procedural autonomy can only be relied upon if the principles of effectiveness and equivalence are satisfied.[164] Thus, we must examine the principles of effectiveness and equivalence. According to the principle of effectiveness, the Member States must ensure that national procedural rules and national remedies do not make it impossible, or excessively difficult, to make a claim based on EU law. Similarly, according to the principle of equivalence, the same procedural rules and national remedies must be equally available for claims based on EU law and claims based on national legislation.[165]

To summarize, it is up to the Member States to construct the procedural rules for recourse and select which national courts have jurisdiction. At the same time, the procedural rules and remedies must be the same for claims on EU law and claims on national legislation. Furthermore, it must not be impossible or exceedingly difficult to make such a claim.

According to Hagemeyer, article 3(5) of the Regulation only enables foreign investors to seek recourse against screening decisions by national authorities. Thus, foreign investors cannot seek recourse against opinions by the Commission, comments by the Member States or information requests by either.[166] Hagemeyer also states that screening decisions will generally be administrative decisions for which the Member States commonly provide redress.[167] With that said, this thesis will not further examine the Member States or the EUs procedural rules for recourse as those are beyond the purpose of this thesis.

With that said, there is another part of recourse for foreign investors which is of interest in the context of this thesis, the lack of a clear definition of the terms *public policy* and *security*. As previously discussed, there is no clear definition of neither public policy nor security in EU law as the Member

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[163] Judgement of 13 December 2017, *Soufiane El Hassani v Minister Spraw Zagranicznych,* C-403/16, EU:C:2017:960, para 26; See also judgement of 16 December 1976, *Rewe,* C-33/76, EU:C:1976:188, para 5.

[164] *Soufiane El Hassani v Minister Spraw Zagranicznych,* para 27.

[165] Opinion of AG Jääskinen delivered on 7 February 2013, C-536/11, EU:C:2013:67, para 3.

[166] Hagemeyer, *Access to Legal Redress in an EU Investment Screening Mechanism,* p. 7.

[167] P. 12

States have a measure of freedom with regards to their national circumstances and individual situations. Because of this, Hagemeyer argues that the Member States may interpret the concepts of security and public order through a discretionary assessment.[168] Hagemeyers argument is supported by Hartmut Krause, at least in the context of German law. According to Krause, it is up to the German government to assess what constitutes public order or public security in Germany. Krause also states that German courts cannot decide whether such an assessment made by the national authorities is correct or not, and that the courts may only interfere against an assessment of security or public order if the decision is such that it cannot be justified.[169] Although what is true in Germany may not be the same in all Member States, the fact remains that national authorities have a lot of liberty in the assessment of threats to security or public order and in the determination of national public order or security. As the concept of public order or security are determined through a discretionary assessment it is unlikely that foreign investors will be successful in seeking legal redress unless the national assessment of public order or security is such that it cannot be justified, such may be the case when screening decisions are revoked for political reasons.[170]

3.7 Confidentiality

The Member State in which territory a FDI is planned or taking place may request information from the foreign investor or the target company, such information shall include, e.g., the ownership structure of the foreign investor and the target company, the estimated value of the FDI and the funding of the investment and its source.[171] The Member State may also pass this information along to the other Member States or to the Commission per request by them.[172]

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[168] Hagemeyer, *Access to Legal Redress in an EU Investment Screening Mechanism*, section 3; See also H. Hestermeyer, ‘Article XXI. Security Exceptions’, in R. Wolfrum, P-T. Stoll, and H. Hestermeyer (eds.), *WTO - Trade in Goods,* vol. 5, Boston, Martinus Nijhoff Publishers*,* 2011, para 21.
[169] H. Krause, ‘Foreign Direct Investment Control in Germany: The M&A Practitioner’s Experience’, in Bourgeois, J HJ. (ed.), *EU Framework for Foreign Direct Investment Control*, Kluwer Law International BV., 2020, p. 83.
[170] Cf. Hagemeyer, *Access to Legal Redress in an EU Investment Screening Mechanism,* p. 17 and 25.
[171] Regulation, arts 9(2) and 9(4).
[172] Regulation, art 9(1); See also Regulation, arts 7(5) and 6(6).

The information made available by the foreign investor or the target company shall be protected by the receivers of the information.[173] Moreover, the information received shall only be used for the purpose for which it was requested.[174] If confidential information is received, the Member States and the Commission shall take all necessary measures to ensure its protection. The information shall not be downgraded or declassified without the prior written consent of the originator. All information that has been provided on a confidential basis should be handled as confidential information.[175]

It follows from the Regulation that the Commission considers the protection of any commercially sensitive information provided by the foreign investor or the target company to the Commission or the Member State to be a high priority. With that said, the system is not without flaws.

It follows from the Regulation that the Member States may request necessary information, if duly justified, in order to provide comments on a FDI if it is likely to affect its public policy or security. As the term duly justified is hard to define, it may prove difficult to distinguish in what situations the other Member States may or may not request information.

Furthermore, a general assumption is that the more parties can access the information, the harder it is to protect it. The EU currently has 27 Member States each of which are obligated by the Regulation to have a contact point for the implementation of the Regulation. The same is true for the Commission making the total number of contact points, in the EU, 28. Furthermore, the Commission shall provide a 'secure and encrypted system […] to support direct cooperation and exchange of information between the contact points'.[176] The safety of this system is outside of the scope of this thesis and will not be commented on. With that said, this means that there are at least 28 contact points which can receive such sensitive information (27 of the Member States plus one of the Commission). Moreover, outside of the concepts of internet security is the concept of corruption. While the EU as a whole performed well in the Corruption Perception Index regarding corruption in the public sector in 2019, there are individual Member States which performed below average.[177]

In conclusion, as it may be difficult to distinguish when the host Member State is obligated to distribute information upon request from other

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[173] Regulation, art 3(4).
[174] Regulation, art 10(1).
[175] Regulation, art 10(2) and preamble 30.
[176] Regulation, art 11(2).
[177] Transparency International, 'CPI 2019: Western Europe & European Union', 23 January 2020 [website]; Commission, 'The Corruption Perception Index 2019: The EU is the best performer in the world', 27 January 2020 [website].

Member States, it follows that it may be difficult to protect the information due to the sensitive nature of the information and the lure of money.

3.8 Closing Conditions

The Regulation does not only affect foreign investors but also the sellers of the shares in the target company. This is illustrated by Krause's arguments in his work *Foreign Direct Investment Control in Germany: The M&A Practitioner's experience* (2020). Krause argues that when a seller is selling their company or shares in their company the seller wants to sell to the best buyer available. In order to establish who the best available buyer is the seller primarily considers the transaction certainty, the price and a good contract, in that order. In this context, Krause refers to 'transaction certainty' as, e.g., a share or asset purchase agreement ('SPA') with as few closing conditions as possible. Furthermore, Krause states that when an investment can be subject to screening mechanisms, the investor will usually seek to protect their investment by implementing closing conditions in the SPA which regulate that the deal only has to be completed if the investment is approved. For the seller, such a condition usually signifies a lower degree of transaction certainty. Therefore, the seller may prefer a different buyer that is not subject to FDI screening mechanisms in order to achieve a higher degree of transaction certainty. Thus, FDI screening mechanisms can become a disadvantage for foreign investors due to the 'necessity' of closing conditions.[178]

Krause's assumption that foreign investors will want to implement closing conditions in the SPA is supported by the opinions of Shaohui Zhang and Yifan Zhang. Zhang and Zhang urge Chinese investors to implement a series of clauses and mechanisms in the SPA in case the investment is refused by the national authorities or in case an unfavorable opinion is issued by the Commission which would allow the parties to exit the investment without indemnity.[179]

To summarize, the Regulation may result in new kinds of clauses and mechanisms becoming standard in SPAs which may result in a lower transaction certainty. As sellers value transaction certainty, they may choose an investor who offers a high transaction certainty but a lower price above one who offers lower transaction certainty but a higher price. In other words, sellers may be more inclined to accept offers from nationals of a Member

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[178] Krause, *Foreign Direct Investment Control in Germany*, pp. 79-80.

[179] S. Zhang and Y. Zhang, 'EU FDI screening and its impact on Chinese investments', Luxemburg, Dentons, 28 May 2018, p. 13.

States or companies registered in a Member State than offers from a foreign investor as a result of the Regulation.

3.9 Forum Shopping

The Commission is obliged by the Regulation to have a publicly available list of the Member States' screening mechanisms.[180] As of the last update on 24 November 2020, 15 Member States have implemented FDI screening mechanisms.[181] As 12 Member States have not yet implemented FDI screening mechanisms, it is clear that not all Member States have the same outlook on FDI which is illustrated by the arguments of Professor Chi-Chung Kao.

Kao argues that the Member States are divided in the questions of FDI screening mechanisms. While some Member States such as France and Italy have considered the issue to be of import, other Member States such as Greece rely on FDI to stimulate the economy.[182] Furthermore, Member States both with and without FDI screening mechanisms in place may process FDIs in different ways due to the Member States different outlooks and opinions on FDIs. Hence, it is natural that some Member States will be more welcoming of FDI whilst others will be more restrictive towards FDI.

As previously mentioned, there is a way for Member States to hinder circumvention of the Regulation when an investment takes place in their territory.[183] However, Member State 'A' cannot decide whether another Member State 'B' shall implement FDI screening mechanisms or if B shall screen an investment in their territory in accordance with B's FDI screening mechanisms or, if B screens a FDI, what screening decisions B shall reach. Although Member State A can provide a comment in this situation, B is only under an obligation to give the comment due consideration, the final decision in relation to the FDI is still the sole responsibility of B.[184]

This difference in attitude and handling of FDI enables foreign investors to "circumvent" the Regulation by establishing themselves in a Member State which does not have FDI screening mechanisms or which embraces FDIs. When the company or subsidiary has been formed in

[180] Regulation, art 3(8).

[181] Denmark, Germany, Slovenia, Spain, France, Italy, Latvia, Lithuania, Hungary, the Netherlands, Austria, Poland, Portugal, Romania and Finland; Commission, 'List of screening mechanisms notified by Member States', 24 November 2020 [online].

[182] C. Kao, 'The EU's FDI Screening Proposal: Can It Really Work?', *European Review*, vol. 28, no. 2, 2019, p. 178.

[183] Regulation, art 3(6).

[184] Regulation, preamble 17.

accordance with the laws of a Member State and has its registered office in the Union, it can rely on the fundamental freedoms such as the freedom to provide and receive services, the free movement of goods and the freedom of establishment in order to conduct business in other Member States. As long as the company or subsidiary is not created and operated through artificial arrangements that do not reflect economic reality, the company is free to invest in other Member States without undergoing any screening. This means that there is a possibility that some Member States will become the base of operations for foreign investors for the direct investments in other, more restrictive, Member States. In this situation, the more restrictive Member States must accept the investment while they have lost the opportunity to control the investment through, for example, restrictive measures such as remedies.[185]

In conclusion, foreign investors may choose to invest in Member States that have more advantageous legislation on FDI screening mechanisms, e.g., no FDI screening mechanisms, with the view of establishing themselves in the Community and perform investments from within the Union.

3.10 Preliminary Analysis

Although the Regulation gives guidance to the Member States regarding their national screening mechanisms, the Regulation does not in fact harmonize FDI screening in the EU. Therefore, foreign investors must adapt to different provisions in different Member States. Furthermore, the Regulation does not harmonize the factors taken into consideration by the Member States when examining whether a FDI is likely to affect public policy or security. Therefore, foreign investors may not be able to predict if their direct investment is likely or unlikely to affect security or public policy. Thus, uncertainty is increased both for foreign investors and for entrepreneurs or entities selling shares. This uncertainty is further increased since there is no universal definition of what constitutes a threat against public order or security in EU law and the question of such an assessment is partly left to the Member States' own subjective determination. Therefore, it may prove difficult for foreign investors to predict what direct investments will threaten public order or security. Furthermore, since Member States may base this assessment on their national needs, it is not entirely clear if guidance from the Court regarding what constitutes such a threat in one Member State is also applicable in another. This subjective determination may leave investors in a

[185] Hindelang, *The free movement of capital and foreign direct investment,* p. 182.

legal conundrum because of which they may choose not to seek legal redress even when available.

Even though the Regulation does not harmonize the factors taken into consideration it does demonstrate some of the factors which the Member States may consider or take into account when determining if the FDI will affect public policy or security. There is one factor which the Regulation indicates is of special import by mentioning it in the preamble and by stating that the Member States should take the factor into account, in particular. This factor is the control of the foreign investor. The Regulation refers to both direct and indirect control, including through significant funding and ownership structure. It is contended that any links between the foreign investor in question and the government of a third country will reflect negatively on the foreign investor in the assessment by the Member States. This can be problematic as there is no definition of state-ownership or state-control and such control can arise from several different situations. For example, we already know from decisions of the Commission that not all ownership from the state amounts to state-control. In this aspect, it is interesting to consider the wording of article 4, according to which the Member States are to take into account both direct and indirect control by the government. Thus follows the question, what would amount to indirect control? Is it for example enough that the company has borrowed large sums of money from a State-owned bank? What happens if public figures hold positions in the government as well as large shareholdings or positions in the board of the foreign investor? What happens if the company is dependent on state-approval in order to act in a certain sensitive sector such as mining or energy? These are all situations which can give rise to close ties between the foreign investor and the government however it is not clear if these situations may amount to indirect control. So far, there exists little guidance on what amounts to indirect control.

Moreover, even if an FDI constitutes a threat against public policy or security it may still be wrong for the Member States to completely prohibit the transaction. Since the principle of proportionality is applicable the least intrusive method to eliminate such concerns must be implemented. Here guidance may be found in competition law which implements remedies to eliminate competition concerns. From competition law follows that such measures must both be proportionate and eliminate the concerns for threats against public policy or security in its entirety.

To summarize, the Regulations raise a lot of questions regarding the factors which should be taken into account without offering substantial guidance to the Member States or foreign investors. This may lead to situations where foreign investors are reluctant to engage in the process of FDI screening which can signify long waiting periods and the disclosure of

commercially sensitive information because they cannot predict with any certainty the screening decision.

With that said, let us now examine an entirely different aspect of the Regulation, the cooperation mechanisms. The host Member State can after notifying the other Member States and the Commission of its intention to screen a FDI in its territory receive comments and opinions. The other Member States and the Commission have up to 50 days, and in some cases longer, to submit such comments and opinions. As foreign investors are likely to want a screening decision from the Member State before closing the transaction, they must account for this timeframe. Moreover, although the opinions by the Commission are non-binding some scholars argue that the Member States will feel compelled to follow them, especially in the context of FDI which may impact programs or projects of Union interest where Member States must take outmost account of the Opinion. This claim is supported by the case law of the CJEU regarding the term *utmost account* from which follows that Member States generally must follow the Commission's Opinion in these matters unless it is not appropriate due to the circumstances of a given situation. However, in that case, the Member States must motivate its decisions not to follow the Opinion. Additionally, the issuance of comments and opinions which are negatively inclined toward a FDI may cause the foreign investor or target company to assume that the screening decision will also be negative. Thus, negative comments and opinions may cause the investor or target company to pull out of the deal during the screening process in order to save time and money. Furthermore, the Commission and the other Member States have 15 months to submit opinions and comments on FDI that have not undergone screening. Such opinions and comments may prompt the host Member States to initiate an *ex-post* review of the FDI (providing the national screening mechanisms allows this). Because of this, foreign investors may take the Member States review process in regard when deciding where to invest.

Furthermore, the cooperation mechanisms between the Member States and other Member States and the Commission mean that sensitive information about the foreign investor or the target company can be made available to up to 28 different contact points. In contrast, in merger control proceedings, sensitive information of the investor or the target company is generally only been accessible to the Commission or the individual Member State in which the concentration is taking place. Although the contact points must take utmost care to keep this information private one must always account for human error and maleficent forces such as hackers. It is not impossible that sellers will take this into account when deciding upon offers or that foreign investors will take this into account when determining what investments to make. For example, in a situation where the foreign investor

presumes that a screening decision will not be positive, concerns over secrecy may drive the investor to not take the chance.

All these seemingly small challenges may together amount to a larger pattern. If foreign investors cannot predict whether their investment will be screened or not, nor what screening decision such screening will probably result in, then transaction certainty would likely decrease. Transaction uncertainty may affect what offer is accepted as sellers generally want as high transaction certainty as possible.

Furthermore, the seller as well as the foreign investor may be affected by the timeframes in the Regulation. Therefore, the timeframes are something that lawyers on both sides of the transaction will have to consider in the deal process and adapt to.

Furthermore, the fact remains that not all Member States have implemented FDI screening mechanisms and the FDI screening mechanisms that exist are not harmonized. Thus, the Member States' different outlook on FDI may cause a situation where foreign investors can 'shop' for the forum which has the most advantageous legislation. However, it is still uncertain if the anti-circumvention mechanisms the Member States may implement can be used to effectively screen investments from within the Union by companies registered in a Member State when those companies are owned or controlled by a foreign investor.

In conclusion, the novelty of the Regulation means that it is still uncertain how FDI screening mechanisms will affect FDIs into the Union. Much remains unclear and it is impossible to accurately predict how the financial market will respond to these new conditions. What is clear, however, is that further guidance is needed from the CJEU and from the Member States themselves.

4 Chinese FDI in the EU

As previously discussed in the background of this thesis, Chinese FDIs into the EU have been a topic of some concern in the media and by politicians. As stated by Changfeng Tu (2019), industrial countries receiving Chinese direct investment have been concerned with the question of whether they will lose their technological advantage towards China due to the sale of technology to China. Additionally, Tu claims that the press in the countries receiving the Chinese direct investments have raised concerns for the loss of domestic jobs due to Chinese takeovers. Even so, Tu argues that it is rare for such concerns to be confirmed in practice.[186]

In keeping with Tu, Sophie Meunier (2019), states that Chinese direct investments into the EU pose various political challenges. Meunier suggests that there are two possible explanations for this phenomenon:

> The first is that Chinese FDI causes political unease because of its novelty. The second is the perception that there is something inherently different about the nature of Chinese FDI and therefore it should not be treated politically like any other foreign investment.[187]

As for the first explanation regarding the novelty of Chinese direct investments into the EU, Meunier states the following. There are other historical examples of when foreign investments have provoked controversy due to the origin of the investor. In these cases, interest in the issue has died down over time. Furthermore, Meunier states that the majority of Chinese direct investments, previously, have been takeovers which are generally considered to be more politically problematic than greenfield investments.

Meunier theorizes that if this first explanation is the cause for the political challenges facing Chinese direct investment then these political concerns will decline 'as Chinese investment projects accumulate and become normalized in a few years'.[188]

As for the second explanation provided, Meunier states in short, the following. Historically, developed economies have invested in developing economies and capital has been a symbol of power. Therefore, the fact that capital is flowing from China into the EU may symbolise a power dynamic whereby China's power is rising while that of the EU is sliding. Furthermore, FDI usually has benefits for the receiving country, e.g., in the form of

[186] C. Tu, 'Chinese Outbound Investments', in W. Lohman and T. Wenninges (eds.), *Chinese FDI in the EU and the US,* Singapore, Springer Nature Singapore Pte Ltd, 2019 p. 4.

[187] Meunier, *Beware of Chinese Bearing Gifts*, p. 345.

[188] Meunier, *Beware of Chinese Bearing Gifts*, pp. 347 and 349.

technological spill-over. However, with some exceptions, Chinese investments seem to be focused on target companies with superior technology, therefore this benefit seems to be flowing in the opposite direction. Moreover, the differences in wages between China and the EU may cause e.g., manufacturing to move abroad thus effecting local employment.[189] Additionally, the nature of the Chinese government and Chinese investors raises concerns regarding the influence of the government over the investors. Concerns are also raised that Chinese companies may have a competitive advantage due to state-backing.[190] Furthermore, security concerns have been raised as the foreign policy goals of China may come at odds with those of the EU.[191] Meunier theorizes that if this second explanation is the reason for the political challenges faced by Chinese direct investment, then more restrictive regulations may be implemented as well as vetting of foreign investment.

4.1 Challenges For Chinese Investors

As previously mentioned, when deciding whether to screen a FDI, Member States can take into account, in particular, if the foreign investor is directly or indirectly controlled by the government of a third country, including through significant funding and ownership structure.

Both private and state-owned Chinese enterprises invest in the EU and worldwide. With that said, 2015, SOEs accounted for the majority of worldwide Chinese cross-border investments at 70 percent in 2015.[192] In the same year, 2015, the value of state-owned Chinese FDI in the Member States was 14 billion euros while the same number for private investment was 6.7 billion euros. Four years later, in 2019, state-owned Chinese FDI in the Member States valued at 1.2 billion euros while the same number for private investment was valued at 10.4 billion euros.[193] Furthermore, the EU-China investment Monitor suggests that over 60 percent of total investments in the EU by Chinese investors since 2000 originate from firms with 20 percent or over government ownership.[194]

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[189] Meunier, *Beware of Chinese Bearing Gifts*, pp. 349-350.
[190] Meunier, *Beware of Chinese Bearing Gifts*, p. 351.
[191] Meunier, *Beware of Chinese Bearing Gifts*, p. 353.
[192] Tu, *Chinese Outbound Investments*, p. 3
[193] Survey by Rhodium Group, cited in C. Textor, ‘Value of Chinese Foreign Direct Investment to EU-28 from 2010 to 2019, by ownership of investment’, *Statista,* 11 November 2020 [online].
[194] SWD (2019) 108 final, p. 60.
S. SWD (2019) 108 final, pp. 56-57 and 60.

However, the fact that a Chinese investor is not state-owned does not necessarily mean that they are not state-controlled. As Tim Wenniges and Walter Lohman, editors of the work *Chinese FDI in the EU and the US: Simple Rules for Turbulent Times* (2019) put it, the Chinese state is heavily involved in the investment decisions of Chinese companies, both private and state-owned. Furthermore, no large investment happens in China without the support of the Communist Party of China.[195] In line with this, the Commission has stated the following regarding the ties between the Chinese government and Chinese acquisitions:

> All Chinese acquisitions could be considered linked to the Chinese government since (1) investments are usually authorised by the government and targeted to specific sectors (e.g. those covering the China 2025 strategy), (2) investments generally involve loans given by Chinese banks (most of them directly controlled by the government).[196]

To summarize, the ties between the Chinese government and private and state-owned enterprises are strong. Thus, it is possible to argue to some degree that all Chinese acquisitions are linked to the Chinese government. As has been established, state-ownership and state-control are factors that the Member States are encouraged to take into account, in particular, when determining if a FDI is likely to affect security or public order.

Furthermore, as follows from the preamble of the Regulation, when the Member States determine how a FDI may affect security or public order, the Member States and the Commission should be able to take into account, in particular, if the foreign investor is pursuing State-led outward programmes or projects.[197] This brings us to 'Made in China 2025'.

'Made in China 2025' is Chinas long-term industrial strategy which was introduced in 2015. The strategy has determined ten specific strategic sectors in which China wants Chinese companies to compete internationally. These are, amongst others, aviation & space equipment, new energy vehicles, energy equipment, medical equipment, robotics, agricultural equipment and railway transportation equipment.[198]

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[195] W. Lohman and T. Wenninges, *Chinese FDI in the EU and the US: Simple Rules for Turbulent Times,* Singapore, Springer Nature Singapore Pte Ltd, 2019 p. vi.
[196] SWD (2019) 108 final, p. 56, footnote 34.
[197] Regulation, preamble 13.
[198] M. J. Zenglein and A. Holzmann, 'Evolving made in China 2025: China's industrial policy in the quest for global tech leadership, no. 8, July 2019, merics: Mercator Institute for China Studies, p. 20.

One way in which China intends to achieve the aim of the strategy is by acquisitions of technology through outward FDI.[199] The ultimate goal of the initiative is to establish China as a world-leading manufacturing power.[200] Some argue that these acquisitions of technology are partly supported and guided by the Chinese state.[201] This argument is supported by the fact that Chinese authorities have guided state-sponsored outbound investments of Chinese companies, much of which is going to the industries recognized in the 'Made in China 2025' initiative as key sectors.[202]

The statistics on Chinese FDI stock in EU as of 2018, by sector shows that in terms of money, the investments are heavily concentrated in the sectors of manufacturing, financial services, mining and leasing together with business services, in that order.[203] Furthermore, the Commission staff working paper (2019) concludes that there has been a surge in the number of M&A deals from China in the EU in the sector of aircraft manufacturing and specialized machinery.[204] Accordingly, China was the second largest acquirer in the aircraft and spacecraft subsector in the EU in 2016.[205] Interestingly, one of the strategic sectors set out in 'Made in China 2025' is aviation and space equipment and another such sector is energy equipment.[206] Regarding state-owned capital, the sectors that have received the most state-owned capital by value is transportation services and logistics, automotive, equipment and components, utilities and real estate.[207]

To summarize, the overall aim of the 'Made in China 2025' initiative is to establish China as a leading manufacturing power. Statistically, the sector which received the most outbound Chinese direct investment in EU countries in 2018 was the manufacturing sector. The third largest sector was the mining

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[199] D. Kempf, 'Investment Relations with China: Never Easy but Always Worthwhile' in W. Lohman and T. Wenninges (eds.), *Chinese FDI in the EU and the US,* Singapore, Springer Nature Singapore Pte Ltd, 2019 pp. 37-38.

[200] UK Trade & Investment: China-Britain Business Council, 'MADE IN CHINA 2025: China Manufacturing in the 21st Century - Opportunities for UK-China Partnership', p. 8; Zenglein and Holzmann, *Evolving Made in China 2025*, p. 20.

[201] J. Wübbeke, M. Meissner, M. J. Zenglein, J. Ives and B. Conrad, 'Made in China 2025: The making of a high-tech superpower and consequences for industrial countries', no. 2, December 2016, merics: Mercator Institute for China Studies, p. 7.

[202] J. Wuttke, 'Simple Rules for a Complex Relationship' in W. Lohman and T. Wenninges (eds.), *Chinese FDI in the EU and the US*, Singapore, Springer Nature Singapore Pte Ltd, 2019 p. 60.

[203] Survey by MOFCOM China; State Administration of Foreign Exchange, cited in C. Textor, 'China's outward FDI stock in EU countries as of 2018, by sector', *Statista,* 11 November 2020 [online].

[204] SWD (2019) 108 final, p. 50.

[205] SWD (2019) 108 final, s. 39.

[206] Zenglein and Holzmann, *Evolving made in China 2025*, p. 20.

[207] SWD (2019) 108 final, p. 60.

sector. This is interesting because the initiative recognized energy equipment as a strategic sector. Furthermore, the sector of aviation & space equipment is recognized by the initiative and a surge in M&A deals in the EU from China has been seen in the subsector of aircraft manufacturing and specialized machinery. Let us examine how this relates to the Regulation. As previously mentioned, Member State may take into account if the foreign investor is pursuing State-led outward programmes or projects when determining if the investment is likely to affect public order or security. Thus, investments by Chinese investors into sectors which are of interest for 'Made in China 2025' may be more likely to undergo screening and be subject to negative screening decisions.

Furthermore, the Regulation mentions the following sectors which the Member States and the Commission may consider the potential effect on when determining if a FDI is likely to affect security or public order:

> critical infrastructure, whether physical or virtual, including energy, transport, water, health, communications, media, data processing or storage, aerospace, defence, electoral or financial infrastructure, and sensitive facilities, as well as land and real estate crucial for the use of such infrastructure;[208]

As demonstrated, the energy and aerospace sectors are considered to be strategic sectors in the Made in China 2025 initiative. Furthermore, the sectors which have received the most state-owned capital from China in the EU is the transport sector and the real estate sector.

4.2 Case Study

As previously discussed, state ownership or control can result from loans from the State. This is illustrated by the case of China National Tire Group.

In 2017, the Commission initiated an anti-subsidy investigation regarding Chinese imports of a certain kind of tires.[209] The Commission found that the development of the tyre industry was actively pursued by the

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[208] Regulation, art 4(1)(a).

[209] Commission, 'Commission implementing regulation (EU) 2018/1690 of 9 November 2018 imposing definitive countervailing duties on imports of certain pneumatic tyres, new or retreaded, of rubber, of a kind used for buses or lorries and with a load index exceeding 121 originating in the People's Republic of China and amending Commission Implementing Regulation (EU) 2018/1579 imposing a definitive anti-dumping duty and collecting definitively the provisional duty imposed on imports of certain pneumatic tyres, new or retreaded, of rubber, of a kind used for buses or lorries, with a load index exceeding 121 originating in the People's Republic of China and repealing Implementing Regulation (EU) 2018/163' (Non-legislative act) ('Commissions tyres act') [2018] OJ L283/1, paras 1-2.

government of China as the government regarded the tyre industry as a strategic industry.[210]

During this investigation, the Commission found that financial institutions in China are directed by the legal environment to coordinate with the government's policy objectives when making financial decisions.[211]

This was for example illustrated by the Commission's findings regarding one of the companies being investigated, China National Tire Group. The China National Tire Group had four exporting producers with varied financial status. During 2014-2016, two of them made profits and had overall positive financial indicators. However, one of these two developed losses during 2017 and signs indicated that all was not good in the financial situation. The third and fourth producers had consecutive years of financial losses as well as worsening financial indicators, yet continued to receive loans at good rates on which they were dependent. During the investigation period, they stopped receiving loans but received support from their parent company in the form of loans taken on their behalf by the parent company.[212] The Commission stated that two of the production companies would not have received further loans at the time of the investigation were it not for State support based on the company's overall financial situation. In this regard, the Commission noted that China National Tire Group is a SOE. Therefore, the Commission treated the outstanding amount of the loans at the time of the investigation as a grant given in order to pursue government policies.[213]

4.3 Preliminary Analysis

According to article 3(2) of the Regulation, the rules and procedures related to the Member States' FDI screening mechanisms shall not discriminate between third countries. Even so, the clear objective behind the Regulation of targeting foreign direct investments made with financial support from the government of a third country and the political challenges which Chinese investors face do raise concern over indirect discrimination based on the nationality of the investor. The Regulation contains several elements which may negatively affect Chinese investors more than other foreign investors. The first of these derives from the factors which the Member States and the Commission may consider when determining if an investment is a threat to public policy or security. On this topic it is interesting to note that there is a

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[210]Commissions tyres act, para 126.
[211] Commissions tyres act, para 189.
[212] Commissions tyres act, para 272.
[213] Commissions tyres act, para 279.

correlation between the key industries which are highlighted by the 'Made in China 2025' initiative and the sectors considered to be critical infrastructure or critical technologies by the Regulation. The sectors of energy, aerospace, health and robotics are for example mentioned in the Regulation. Correspondingly, the 'Made in China 2025' initiative mentions sectors such as energy equipment, aviation & space equipment, medical equipment and robotics. Thus, one must ask the question of whether Chinese investments, made in accordance with the initiative, will be more likely to be screened due to this parallelism in the initiative and in the factors mentioned in the Regulation.

Moreover, when determining if a FDI is likely to affect security or public order, the Member States and the Commission can take into account, in particular, if the foreign investor is controlled by the State of a third country. Furthermore, they may take into account whether the foreign investor is controlled through significant funding or is pursuing State-led outward projects or programmes. As established above, the Chinese government has close ties to Chinese companies, both private and public. The government is generally involved in all large investments from Chinese companies as these generally involve authorization by the government and target the specific sectors covered by the government's state-led outwards programmes. Furthermore, most large investments require loans from Chinese banks which are usually controlled by the State.

It follows from the case study that loans granted to Chinese companies can in some situations be considered as grants given in order to pursue government policies. In the case study the company which received the loans on behalf of its subsidiary was state-owned, operated in an industry which the government considered to be a key industry and would likely not have received loans based on the subsidiary's financial situation. The question is thus if such grants could be considered as significant funding which constitutes state-control? In the case of China, it is likely that the answer to such a question would be yes, at least if the company in question was operating in one of the sectors set out in 'Made in China 2025'. This is because state-control in such a situation is indicated by (1) state-ownership, (2) significant funding and (3) the investment is in pursuit of state-led outwards programmes, i.e., 'Made in China 2025'.

Furthermore, it follows from the work of scholars and news articles that Chinese investments in the EU face political challenges and raise concerns amongst the general public. This may be because China is still a relatively new player in the investment scene of the Union or because Chinese investors are perceived as different from other types of investors. If the political challenges derive from the novelty of Chinese investors, then it is likely that they will subside with time. If, however, the challenges derive from the nature of Chinese investors then, as Meunier predicts, we may come to see more

restrictive legislation in future. On this subject, it is interesting to note that the Commission has recently (2020) adopted a white paper regarding foreign subsidies in the EU in preparation for a legislative proposal.[214] So why is this an issue? If the political concerns derive from the novelty of Chinese direct investments then those concerns should, as already mentioned, decrease with time. If, however, the second explanation is the reason for such concerns, then this may affect the comments by other Member States and the opinions of the Commission, and therefore the host Member State as well as the host Member State is obligated to give such comments and opinions due consideration by, where appropriate, undertaking measures. As previously discussed, if the opinion from the Commission regards an investment that may affect programmes or projects of Union interest, the host Member States may be reluctant to diverge from such an opinion. Therefore, the public opinion of Chinese direct investments may come to affect the national screening mechanisms and screening decisions.

To summarize, Chinese direct investments differ from other types of FDIs into the EU because of the close ties between the Chinese government and companies, because of the State-led programmes 'Made in China 2025' and because of the public opinion regarding Chinese direct investments. For these reasons, the Regulation may come to affect Chinese investors more than other foreign investors. As illustrated previously, Chinese M&A deals may therefore include more closing conditions thus lowering the transaction certainty. These factors lead to the conclusion that sellers may be less inclined to sell to Chinese investors because of concerns for public opinion and because of lower transaction certainty due to FDI screening mechanisms.

[214] COM (2020) 253 final.

5 Conclusion

The main analysis and findings of this thesis are presented and summarized in the chapters two to four, particularly in the preliminary analyses. This section will further summarize the conclusions drawn from this thesis as well as the opinions of the author of this thesis.

The main purpose of this essay was to examine which investments are within the scope of the Regulation and what challenges the Regulation may present for foreign investors.

Regarding what investments are within the scope of the Regulation, the opinion of this thesis is the following; When determining if an investment falls within the scope of the Regulation, foreign investors should consider the total shareholdings they acquire through the M&A deal. In other words, if the foreign investor already has shares in the target company, which do not enable them to have control over the company, even a small acquisition of shares or voting power in the target company may enable them to have effective control over the target company. Therefore, the total amount of shares or voting power the foreign investor holds after the investment should be taken into consideration when determining if an investment is a direct investment which falls within the scope of the Regulation. With that said, the foreign investor should assume that total shareholdings of above 10 percent may invoke interest from the Member States, regardless of if the investment is in fact a direct investment.

Likewise, this thesis proposes that foreign investors should consider the purpose of the deal, such as if they aim to participate in the management of the target company, when determining if the investment is a direct investment. In doing so, factors such as the members on the target companies board of directors, the senior executives of the target company and trade or loans between the foreign investor and the target company post the acquisition should be considered.

As this thesis has demonstrated, much remains unknown about the practical effect the Regulation will have on foreign investors. With that said, this thesis concludes that Chinese investors are particularly exposed to the challenges posed by the Regulation. It is the opinion of this thesis that Chinese investors are particularly exposed to the challenges, partly, due to the political challenges their investments face in the EU and, partly, because of the factors which the Member States are encouraged to consider or take into account by the Regulation. It is no secret that the Chinese state has a lot of influence over Chinese companies and such companies' investment decisions. Therefore, this thesis proposes that it is reasonable to expect such investment decisions to, *generally*, comply with the Chinese states' investment policy or State-led

outward programmes such as the 'Made in China 2025' initiative. The analysed data, for example, shows that Chinese investments have surged in the sector of aircraft manufacturing. In the same way, the analysed data shows that the sectors of transportation services and logistics and automotive have received the most state-owned capital. The 'Made in China 2025' initiative recognizes the sectors of aviation equipment, railway transportation equipment and new energy vehicles. Therefore, this thesis argues that it is reasonable to expect Chinese companies to invest in the sectors which the initiative recognizes as key sectors. While the data analysed in this thesis is not sufficient to draw a definite conclusion, the hypothesis is further supported by literature. Thus, this thesis argues that it is fair to assume that Chinese investors will continue to invest heavily in the sectors included in the initiative. Now you may ask, how does this tie into challenges posed by the Regulation? Well, several of the sectors recognized in the initiative are also recognized in the Regulation. In the case of the Regulation, however, the sectors are recognized as critical infrastructure or critical technologies which the Member States and the Commission may consider the potential effect on when determining if a FDI is likely to affect security or public order. It is the opinion of this thesis that this similarity between the initiative and the Regulation creates a cycle: Chinese investors are *likely* going to continue to invest in the sectors mentioned in the initiative and the Member States are *likely* to be more inclined to screen investments into critical infrastructure or critical technologies. This thesis suggests that this cycle may cause Chinese investments to be screened more often than other types of FDI and that it may also affect screening decisions.

Furthermore, this thesis suggests that Chinese investors are likely to have close ties with the Chinese government, for instance, through loans or state-ownership. This suggestion is supported by literature. In addition, the Commission has previously recognized these close ties in a working document in which was stated that all Chinese acquisitions could be considered linked to the Chinese government. As the Regulation encourages Member States and the Commission to take into account, in particular, if the foreign investor is controlled by the government, either directly or indirectly, it is in the opinion of this thesis clear that this factor will be important, either in screening decisions or in opinions by the Commission.

This thesis suggestion, that Chinese investors are particularly exposed to challenges by the Regulation, is further supported by the fact that Chinese investments in the EU have already met with political challenges, as argued by Meunier and Tu and demonstrated by the press. Therefore, it is the opinion of this thesis that all these elements put together (the political challenges and the factors mentioned in article 4 of the Regulation), seem to indicate a bigger pattern where Chinese investors will have a harder time investing in the EU going forwards. With that said, however, while the pattern may become the

general case as concluded by this thesis, it can be undermined by so-called forum-shopping which could allow foreign investors to circumvent screening mechanisms.

One thing that is completely clear is that the Regulation does not compel Member States to screen FDI nor does it dictate what the screening decision from such screening shall be. As previously discussed, there are some ways for Member States to screen investments from within the EU, however, this should not be considered the norm as companies registered in the EU and nationals of the EU can, generally, rely on the fundamental freedoms. Therefore, this thesis suggests that we can end up in a situation where foreign investors may feel compelled to invest in Member States which have no FDI screening mechanisms in place, for instance with the intent to register a subsidiary within the Union. Similarly, the Member States outlook on FDIs differs, and while some Member States may be more negatively inclined, others may be more positively inclined towards FDI. Thus, this thesis suggests that that foreign investors will aim to 'shop' for the right forum, i.e. Member State, to invest in. Such a situation is not unheard of, as demonstrated by the Principle of prohibition of abuse of rights. How the Member States and the Commission aims to deal with this question remains to be seen.

With that said, this thesis also suggests that foreign investors should not assume that investments made through subsidiaries, such as special-purpose entities, registered in the EU will not be screened. To the contrary, it is the opinion of this thesis that the definition of a SPE is quite similar to the description of a company whose direct investments may be screened under article 3(6) of the Regulation. Therefore, this thesis urges foreign investors to consider if their subsidiary fits the definition of a SPE registered in the EU before making any direct investment through said subsidiary.

Likewise, this thesis suggests that there is room for separate transactions to be considered as a single transaction, and thus a single investment, in the context of FDI screening in the case where a foreign investor transfers capital to a subsidiary in the EU and the subsidiary then uses said capital to make a direct investment, thus allowing for screening under article 3(6) of the Regulation. However, as previously mentioned, this theory is not supported by literature and must therefore be further examined by scholars and legal experts before any conclusion can be drawn on the basis of this argument. With that said, it will be interesting to see how the CJEU will deal with circumvention of the Regulation and forum shopping.

Finally, this thesis concludes that while foreign investors can find guidance on the factors of import for the determination of threats against public policy and public order, more guidance is needed from the individual Member States regarding the national security needs of their state. Moreover, it is also the opinion of this thesis that guidance is needed from the Court

regarding what remedies are proportionate and appropriate in order for foreign investors to be able to prepare for screening mechanisms and screening decisions.

All things considered, this thesis suggests that, the area of FDI screening mechanisms in the EU will evolve rapidly in the coming years. In the meantime, however, there is need for scholars and legal experts to continue to monitor changes in this fast-developing area.

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