The new EU Regulation 2019/452 on foreign investment screening: Protective, not protectionist

1. Background

The EU legal order has long protected investors' rights: Article 63 of the Treaty on the Functioning of the European Union ("TFEU") protects free movement of capital, granting rights to EU and non-EU investors. However, the TFUE allows Member States ("MS") to vet foreign investment on public policy grounds. Striking a balance between protecting investors and MS legitimate interests, the Court of Justice of the EU has developed a body of case law on the various national screening systems.

In an effort to harmonize the different national screening systems, in September 2017, the European Commission (the "Commission") presented a proposal for a regulation on a foreign investment screening framework.[1] On 19 March 2019, the proposal became law ("Regulation 2019/452").[2]

Regulation 2019/452 shall apply from 11 October 2020, but its effects may already be felt today and, in any event, investors need to prepare for the new reporting obligations, as described below.

2. Key provisions of the new Regulation 2019/452

a. Annual reporting obligations for all MS

All MS will have to submit to the Commission an annual report with aggregated information on foreign direct investment ("FDI") taking place in their territory and information on the application of their screening mechanisms (Article 5).

- Based on the data submitted by MS, the Commission will publish an annual report on the implementation of the Regulation.
- The first report will thus cover investments completed in 2020.

b. Requirements for a valid national screening mechanism

Codifying existing principles, the Regulation sets out the requirements for a valid screening mechanism (Article 3), such as

- transparency of rules and procedures (e.g. relevant timeframes; clearly set out the grounds for screening),
- non-discrimination among foreign investors, confidentiality of information exchange, and
- the possibility of recourse against screening decisions.

c. Screen-able investments

A FDI is likely to fall within the scope of a national screening mechanism when it concerns one of the following areas (Article 4):

- critical infrastructure,

[1] See our previous newsletter of 8 September 2017 (http://www.gop.it/doc_pubblicazioni/683_c5clpu4kya_ita.pdf)

[2] Available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R0452&from=EN

- critical technologies,
- supply of critical inputs, such as energy or raw materials,
- access to sensitive information,
- freedom and pluralism of the media, and / or
- when 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.

d. Cooperation mechanisms

The Regulation provides for cooperation between MSs as well as with the Commission (Articles 6 and 7).

- In particular, a MS can provide comments to the MS where the investment takes place, when it considers that the investment is likely to affect its security or public order, and/or
- the Commission can issue an opinion, when it considers that the investment is likely to affect security or public order in more than one MS.
- The Commission will be obliged to issue an opinion, if at least one third of the MS express concerns.

The timeframe is as follows:

- MS and the Commission have 35 days from the notification of the screening carried out by another MS to provide their comments/opinion.
- However, MS and the Commission can request additional information within 15 days of the notification and then deliver their comments/opinions within 20 days of receiving the additional information.
- Instead, if the investment is not undergoing screening, MS and Commission have 15 months after the FDI has been completed to provide their comments/opinion.

MS' comments and Commission's opinions will not be binding on the MS reviewing the FDI. The final decision will thus remain the prerogative of that MS. However, *due consideration* shall be given by the reviewing MS to the comments and opinions received.

e. Commission power to issue opinions in case of FDI affecting EU projects

Finally, the Commission can issue an opinion ex officio also when the investment is likely to affect projects or programs of Union interest on grounds of security or public order (Article 8). In particular, projects and programs of EU interest include:

- programs receiving EU funds, such as Horizon 2020, and
- programs covered by EU law on critical infrastructure, technologies or input.

In this case, the MS has to take *utmost account* of the Commission opinion and provide an explanation if the opinion is not followed.

3. Conclusive remarks

MS remain sovereign in terms of screening FDI, with Regulation 2019/452 essentially seeking to harmonize different regimes and to create more cooperation between MS. However, MS which are still without a screening mechanism may be under "peer-pressure" to set up one.

Advices for foreign investors

- ✓ Be aware of the existing national screening procedures (if any), especially when the investment falls under the critical sectors and proceed to a full **assessment of risks in advance**
- ✓ Be aware of the extra time the FDI screening process may involve in addition to the traditional transaction steps (i.e. market screening, financial advice, DD, negotiation, SPA)
- ✓ Be aware that even post-closing FDI screening may occur. Therefore, **be prepared for a worst case scenario in the SPA**, including the necessary contractual remedies

Please note that the above is simply an overview of the subject matter and it is not, nor is it intended to be, a legal opinion or legal advice. Should you have any questions concerning the new law's requirements set out above or should you wish to receive information on our annual package, please do not hesitate to contact us.

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