THE EUROPEAN UNION: A BATTLEGROUND FOR COORDINATING SCREENING MECHANISMS

Interview with Paul Lignières, Doctor of Law, Vice-Chancellor of the Catholic University of Paris, honorary lawyer

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Three years after the introduction of the European mechanism, what are your thoughts on its philosophy? Has it achieved its objective?

Paul Lignières: Over the last few years, the European Union has radically changed its approach to foreign investment. In the past, the European Commission had always been against national controls on foreign investment. This is why France was condemned by the then European Court of Justice (ECJ), now the Court of Justice of the European Union (CJEU) in 2000 for requiring the Church of Scientology to obtain prior authorisation for foreign investment. And when, in 2006 during the merger between GDF and Suez, the French Prime Minister announced that the French government would use the golden share mechanism to retain strategic assets, the European Commission made it clear that it was not in favour. It considered that golden shares were not compatible with EU law and that they had no place in the single market. However, golden shares can be compatible with EU law, and the Commission later admitted this.

Things began to change following a series of opportunistic and unplanned national initiatives in around 10 Member States. In France, this included the Montebourg Decree in 2014 when GE took control of Alstom's energy division. At the time this decree was adopted, it was described by the vast majority of French legal doctrine as pure heresy with regard to EU law. It is therefore particularly remarkable that today this mechanism is not only accepted but also promoted by the Commission, which sees it as a model, and that it is accepted by almost all legal experts.

The EU had three objectives in making this turnaround: (1) to provide a framework and consistency to all national regulations; (2) to encourage Member States to take action against the predatory behaviour of certain countries with regard to investments in strategic sectors; and (3) to impose reciprocity, particularly with regard to China, whose market is not really open.

The first objective has been a real success because national regulations are now more consistent. The second objective has also been achieved, even if this defence against the predatory behaviour of certain countries needs to be permanent. Member States have taken action, and naivety has often been replaced by a more watchful eye on companies from certain countries. An increasing number of EU countries are setting up control mechanisms.

However, the third objective has not been achieved. Reciprocity has been overlooked in the EU's response, and it remains a totally taboo subject at EU level. Without explicitly stating why, the EU systematically blocks attempts to introduce reciprocity into its legislation, even though WTO law allows it. In France, the issue remains unresolved. The matter was originally raised during parliamentary debates on the PACTE Law, but was refused by the government on the grounds of France's "international commitments". China and the EU have opened the debate within the framework of their investment agreement. Progress has been made in the area of international trade transactions, but nothing has been achieved in the area of public procurement. Lastly, if the reciprocity mechanism had been introduced for foreign investments, France could have given certain foreign investors the same sometimes hostile treatment that French investors receive in foreign countries. In practice, this could have led to investments being refused where there was no reciprocity. There remains a real gap here between political declarations and actions. This is unfortunately a perfect illustration of some of the criticisms levelled at the EU, which lacks transparency and is too far removed from the needs of the people.

Has the EU struck a satisfactory balance yet between respect for the sovereignty of member states and the necessary protection of the Union and its principles?

Paul Lignières: Without any hesitation, the answer is yes. The European Commission's work in this area is exemplary. It has found the right balance in its regulation (Regulation (EU) 2019/452), its approach has been very measured and highly intelligent. The Commission has been exemplary in the way the European regulation has been adopted. It had previously pointed out that the many national initiatives were not always the best ones, that these often led to inconsistent results and that there was a risk that some Member States could go too far. The Commission's preference was therefore to intervene and establish a framework, with the consent of all Member States. This is a good example of a successful "bottom-up" approach: a European regulation that was in fact born out of national initiatives and that did not give the impression that the EU was imposing something that was unrelated to the needs of the people. This type of intervention by the EU is naturally much better received than initiatives that challenge national legislation.

This approach could inspire a reform of EU competition law. It is well known that this law does not currently take sufficient account of the issues surrounding the industrial sovereignty of Member States. It is possible that in the future the EU will follow the same line of thinking as it has with investment control. In other words, faced with a proliferation of national initiatives, it will introduce a reform that leads to harmonisation. In this scenario, the reform and development of European foreign investment law would be a form of best practice for other areas.

Coming back to foreign investment, to what extent does the Commission's own responsibility dovetail with national responsibilities?

Paul Lignières: The Commission has assumed the responsibility of coordinating Member State initiatives. It is a rather light-touch mechanism, in the sense that Member States have to consider the questions posed by the Commission, but they remain sovereign. They retain their decision-making power. So State sovereignty is not infringed. The Commission applies the principle of subsidiarity, which has sometimes been neglected in the construction of Europe: it only intervenes to regulate trade between Member States and to promote coordination among their actions. In actual fact, it encourages each country to exercise its national economic sovereignty, thereby protecting European economic sovereignty.

Does French foreign investment law protect investors? Is it compatible with EU law?

Paul Lignières: We need to keep in mind that the mechanism includes a part that remains under State control. It will always, in my opinion, retain a part that is not covered by law, where the ultimate freedom of the Member State to exercise its sovereignty is tucked away.

The role of the State is always represented, from several angles. Firstly, the State will always try to delay the triggering of deadlines in certain cases. This is the usual approach with regard to the completeness of the file (if the file is incomplete, the deadline does not start running). Secondly, if you ask the State to comply with the deadline set, it can still issue an authorisation with unacceptable conditions that need to be negotiated. The State will then explain that it has not met the deadline because you did not accept the conditions!

Do you think that there is also an overriding political issue that might influence how certain transactions are handled without making it clear, for example the takeover of Carrefour by Couche-Tard in France?

Paul Lignières: The instrumentalisation of foreign investment control cannot be ruled out. It is quite natural to use FDI control to defend against a hostile takeover, which is certainly what Carrefour did. Having used investment control and related arguments as a defence to hostile

takeovers myself, I can see that some ideas that seemed unacceptable a few years ago are becoming common practice today. Political sensitivities have changed and with them the direction of control. For example, 15 years ago, the very idea of amending the Foreign Investment Decree to include the drinking water sector caused such an uproar within the company it was protecting and among its legal counsel that the idea was immediately withdrawn. Today, a legal counsel would be blamed for not thinking of such a possibility in such a case.

The intuition of politicians, who are answerable to their constituents and in touch with the real world, can carry more weight than a purely intellectual and technical approach in Brussels. This is why I do not think we should try to exclude the political aspect of these issues altogether. These approaches lead us to the conclusion today that not all foreign investment is necessarily good. Financial resources are not that scarce. It is therefore right to be wary of certain investors, and sometimes it is necessary.

Despite the fact that these transactions are now highly regulated, investors have a good image of France. France is seen as a country that is very open to foreign investment, and in practice it is. Nevertheless, there are still rules in certain sectors that can be explained more by corporatism than by the defence of sovereignty. I am thinking of the health sector in particular (laboratories, pharmacies, veterinarians, and so on) but also the legal sector (notaries, lawyers and certain rules concerning the legal profession). Similarly, in the infrastructure or energy sector, some investors may rightly think that pricing issues, which are still very political in France (despite the existence of regulatory authorities), may favour French investors over foreign investors (the former being more comfortable bearing political risk than the latter). Moreover, the jurisdictional framework of State decisions is not regarded as a sufficient guarantee, in particular because foreign investors tend not to trust the French Council of State, perceived as a judge close to the State and more political than legal. The French government has not relinquished strategic decisions in regulated sectors, which automatically leads to a lack of legal security. Here again, there is a question of State control and the law is not the be-all and end-all.

However, this political and sovereignty is limited, intermittent and not systematic. If it were, it could lead to a risk of loss of reputation for the French government and its word. The loss of investor confidence in the word of the French government would undoubtedly be immediately reflected in the cost of public debt.

Despite the relatively strong influence of politics, the European and French investment regulations are considered to be very well developed. International investors are generally not particularly worried about this when it comes to implementing a sound economic venture. In fact, my foreign clients never understood why, prior to the 2014 regulations, France was so lax on investment control. The current control mechanism is relatively inexpensive and can be implemented with limited documentation and within a reasonable timeframe. Overall, such a mechanism is more reassuring for the foreign investor than no mechanism at all, which would open the door to politicking and suspicion. I remember an Asian investor who insisted on obtaining authorisation from the French government for his investment even though it did not fall within the scope of the law on foreign investment control.

Can the sharing of information between Member States, as recommended by the European mechanism, be misused by some of them (being less demanding so as to position themselves strategically in relation to other States)?

Paul Lignières: In practice, the mechanism is not particularly binding on Member States and few if any sanctions will be imposed as a result. The suggestion that a Member State may not fully comply with its duty to share information may ultimately be a case of it exercising its autonomy and sovereign will. It would therefore be wrong to say that Member States are hijacking the European information sharing system.

It is possible to argue that if States do not always find all the information they might want, it is because some of the missing information is confidential.

Again, however, this logic has its limits. The argument of the sovereignty of the State and its constitutional powers to keep certain information secret cannot be invoked indefinitely. The weakness of this justification for exempting the State from its duties is obvious when we consider the loss of credit incurred if it were to resort to it too often.

Moreover, in France, for example, this sovereignty logic may be limited by the fact that the French Ministry of Finance and the relevant supervisory ministry have an opposing view of the issues. Finance ministers may be happy to welcome a foreign investor that another ministry would prefer to reject to preserve some kind of sovereignty.

This also helps to explain why it is essential to centralise control at the French Treasury, to prevent decision-making centres from being spread too thinly, thereby encouraging the influence of "evening visitors".

Conversely, we might also ask whether a Member State could play the minimum requirement card to attract foreign investors. This could happen, but we must not lose sight of the fact that today this right is not seen as a significant constraint for foreign investors, and some are even reassured that it exists. Therefore, it seems to me that a State could not use the argument of its flexibility or freedom from rules to attract investors.

Is the principle of non-discrimination between foreign investors fully followed in practice?

Paul Lignières: This question is linked to that of reciprocity.

There is no principle of reciprocity in relations with certain States, but the fact remains that the French government may occasionally have a legitimate interest for treating investors differently depending on their country of origin.

As regards the principle of reciprocity, European law has taken away Member States' sovereign powers without giving them the necessary means to protect themselves against certain investments. To compensate for this vacuum, Member States have to interpret the rules as flexibly as possible in order to exercise their sovereign powers.

The different treatment afforded to investors by non-EU States requires the EU and its Member States to be particularly vigilant. The response from EU States must be pragmatic, effective and compatible with EU law, which is not easy. But, as I explained above, the French government – like all EU Member States – has the practical means to restrain an investor who is not wanted because of their nationality. Does the French government use these means? Whether it does or not is a matter of professional secrecy, but it is reasonable to assume that the mere fact they are available may be sufficient to dissuade the unwanted investor.

How does the EU mechanism compare with the one in the United States?

Paul Lignières: The French and EU control mechanism is much simpler than that in the United States. How they are used is also different. In the United States, it is customary to prepare an extensive file in conjunction with an expert in the foreign investor procedure, whereas in France, the files are very simple and experts are not always necessary. The EU is therefore more welcoming to US investors than the other way round.

To what extent is the strengthening of FDI control necessary in times of crisis?

Paul Lignières: There are two aspects to my conclusion on the role of foreign investment control in times of crisis.

Firstly, the crisis highlights what is vital; it acts as a revealing factor. We discover new sensitive sectors that we were not previously aware of. Certain activities, products or services become essential for the continuity of economic and social life. I realised four years ago that it was essential to protect sectors such as agri-food or certain parts of the property sector, given what they contribute to the French economy. It may also be appropriate to protect new sectors such as education. The risk of waiting to extend State protection to these sectors is that we may be forced to do so in response to major takeovers.

Secondly, the crisis inevitably turns certain activities into easy prey. Foreign investors see companies weakened by the crisis as creating a windfall effect against which it is only natural to seek protection. The European Commission is well aware of this idea and is trying to promote State aid in such cases.

So, yes, there is no doubt that crises are times when it may be essential to strengthen foreign investment control and this is what the French government did during the Covid pandemic.

To what extent does the disparity of national systems pose a risk for France?

Paul Lignières: I have never seen a French investment blocked at the intra-European level by these mechanisms, nor a foreign investment switch to a country outside France because of French investment control regulations. Consequently, I don't see why the differences between the mechanisms at the EU level would be a problem.

What improvements would you have suggested for the EU mechanism?

Paul Lignières: The rules and recommendations put in place at the EU level are highly relevant, but they also need to be highly flexible because the market and practices change. In my opinion, strengthening control of the mechanisms put in place would provide real added value, in particular by expanding the scope to new sectors such as property or education. It would be valuable to set up a body to continually and regularly evaluate the effectiveness of these mechanisms, taking into account recent developments in practice and the needs of Member States. Furthermore, it is important to be able to react very quickly in the event of a crisis and to ensure that EU rules have not blocked any country. Lastly, it is absolutely necessary to allow Member States to introduce the principle of reciprocity into their laws to block investments by companies from countries that do not welcome European investors.