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**CECIMO Position Paper: EU Proposal for a Regulation establishing a framework for screening FDI into the EU**

**Summary**

This paper sets out the position of CECIMO, the European Association for the Machine Tool Industries, concerning the proposal for a foreign direct investment (FDI) screening mechanism for the EU.

CECIMO welcomes the European Commission's (EC or Commission) efforts to protect the essential interests of the Union, by attempting to ensure more legal certainty and imposing a minimum set of requirements (transparency, non-discrimination and right to judicial redress). Hence, the regulation promotes a move towards a more harmonised approach across the EU. We value that the ultimate decision on FDI is taken by national governments and agree that the EU needs to remain an open market for FDI, as it is a crucial source of growth and employment.

The regulation will assist harmonisation and transparency, but it should be noted that Foreign Direct Investments are not necessarily due to the lack of this regulation, as the main target for Chinese FDI, for example, are the Big 3 (UK, Germany and France) countries, which already have screening mechanisms in place for FDI.

The regulation risks allowing political pressure to be exerted among Member States (MS). The MS are not compelled to follow the opinions of the Commission, but the consequences of not doing so are also not clear. Moreover, given the cross-border nature of value chains, interested MS can put pressure on others – for instance, where the FDI takes place – and jeopardise another country's sovereign competence to decide on the matter.

The proposal needs a better-defined scope to avoid misinterpretations across Member States. The broad definition of "investment" includes investments for small manufacturers and start-ups whose business decisions might be systematically undermined by national and EU interventions. The lawmakers should give more guidance for the interpretation of security and public order, while more business-friendly issues, such as FDI reciprocity, need to be dealt with in investment agreements.

The Investment Screening Coordination Group will enable information sharing and transparency. In practice, however, involving so many stakeholders will make it extremely difficult, if not impossible, to preserve the confidentiality of commercially-sensitive information to competitors and the public. This not only puts additional pressure on governments, which might be taking an unpopular decision, but it may also undermine future relationships with third-country investors, which is the exact opposite of what the regulation aims to achieve.

## Recommendations

- CECIMO expects a clearer explanation of “due consideration”, when taking into account MS and Commission opinions.
- Legislators should take in account the global nature of today’s value chains and reduce uncertainties and political pressure on business decisions.
- The scope of the Regulation needs to be fine-tuned to avoid differing interpretations across Member States – especially regarding “justified reasons” for a country to intervene, requesting information and the consequences for not fulfilling requests.
- More attention should be paid to the issue of the reciprocity in investment relationships with third countries.
- To minimise the risk of leaking commercially-sensitive information, communication channels in the Investment Screening Coordination Group must be properly secured and special confidentiality obligations should apply to its members.

## Background

Until now, there has not been a mechanism for screening Foreign Direct Investment (FDI) at EU level. At present, 12 EU countries have some kind of screening mechanism in place, functioning on the grounds of national security.

Although the debate is not new, it has gained momentum due to rising concerns over specific Chinese acquisitions in strategically important sectors: infrastructure, media, artificial intelligence and other key enabling technologies. As a result, political actors expressed the potential need to create a screening mechanism at EU level.

That is why, in his State of the Union speech on 13 September 2017, EC President Jean-Claude Juncker invoked his intention to protect European strategic interests and announced the proposal for a new EU framework for investment screening. He made an explicit reference to foreign state-owned companies willing to invest in the EU. On May 28, the European Parliament’s (EP) Committee on International Trade adopted the report based on which the EP will negotiate. And, on June 13, the Council of the EU (Council) also agreed on its negotiating position, with Triologue discussions started on July 10 between the EU institutions.

## The EC proposal<sup>1</sup>

- The EC regulation creates a common framework for screening FDI in the EU, on grounds of national security or public order.
- It sets basic requirements and timeframes for the Member States to perform the screening procedure.
- It proposes a non-exhaustive list of factors to be taken in consideration during the screening.
- It specifies that it does not oblige the MS to create a national screening mechanism and, more importantly, that the final decision lies with the MS.

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<sup>1</sup> The Proposal for a Regulation of the European Parliament and of the Council establishing a framework to review FDI’s into the EU is available here: [https://ec.europa.eu/info/law/better-regulation/initiatives/com-2017-487\\_en](https://ec.europa.eu/info/law/better-regulation/initiatives/com-2017-487_en)



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- It creates an obligation – both for Member States that have a screening mechanism in place and those without such mechanism – to report annually on FDIs that took place in their territory. The states already having mechanism will also need to report on how they apply it.
- It creates a cooperation mechanism between MS and the EC, aiming to improve information exchange on planned and completed screenings under national mechanisms and increase coordination on these kinds of decisions.
- It opens the possibility for the EC to perform FDI screening if it affects the security and public order in one or more MS.
- It creates the responsibility for the MS to inform the EC and other MS about FDI screenings falling under the scope of the regulation. Any MS or the EC can then issue a non-binding opinion regarding a particular FDI.
- It sets up an Investment Screening Coordination Group, chaired by a representative of the EC, with other MS representatives as members to exchange information on FDIs.

### The European Parliament's position<sup>2</sup>:

- The EP makes an attempt to define the scope of the regulation and proposes other definitions. For instance, it introduces the concept of direct/indirect links, or direct/indirect control. It provides a definition for “foreign government-controlled direct investment”.
- It gives a non-exhaustive list of examples of critical and strategic infrastructure, as well as technologies.
- It stresses the importance of guaranteeing the highest level of protection for confidential or commercially-sensitive information.
- It underlines the necessity to not create prejudice through unreasonable delays.
- It insists that the information requested by the Commission or the MS shall be **the best** information available (accurate, comprehensive and reliable).<sup>3</sup>

### The Council's position<sup>4</sup>

The Council welcomes the Commission's initiative to protect the EU's strategic sectors, while keeping the EU open to investment.

### CECIMO's position

CECIMO welcomes the EC initiative to protect the essential interests of the Union. We agree with the legislators that the European market needs to remain open to foreign direct investment, considering its positive impact on growth and employment.

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<sup>2</sup> The European Parliament's press release can be found here: <http://www.europarl.europa.eu/news/en/press-room/20180528IPRO4446/foreign-investment-to-be-screened-to-protect-eu-countries-strategic-interests>

<sup>3</sup> The European Parliament's report on the proposal for a regulation establishing a framework for screening of foreign direct investments into the European Union can be found here:

<http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-%2f%2fEP%2f%2fNONSGML%2bREPORT%2bA8-2018-0198%2b0%2bDOC%2bPDF%2bV0%2f%2fEN>

<sup>4</sup> The press release of the Council can be found here: <http://www.consilium.europa.eu/en/press/press-releases/2018/06/13/screening-of-investments-council-agrees-its-negotiating-stance/>

We understand the intention of ensuring a more harmonised legal framework across the Union by defining a minimum set of requirements, such as non-discrimination among third countries, transparency requirements and the right to seek judicial redress (article 6). At the same time, we appreciate that MS that do not have a screening mechanism are not obliged to adopt it. The primary screening of investment based on national security and public order should continue to be tackled at the MS level with intervention at the EU level based on information disclosure and transparency so that the legitimate security and public order concerns of another MS or the EU as a whole can be considered.

CECIMO values that the ultimate decision was left to the MS that is the recipient of FDI. We also note the efforts to limit the scope of the regulation to matters of national security and public order.

Nevertheless, this Regulation lacks important elements and fails to deliver its purpose in the following aspects:

**1. The regulation is necessarily a compromise, as the ultimate decision on FDI rests with the Member State which raises questions on its general usefulness**

The proposal is a result of rising concerns over Chinese state-owned companies purchasing critical EU assets, such as cutting-edge technologies, dual-use goods, infrastructure projects, etc. It was therefore thought that we need a screening mechanism to prevent such buy-outs and protect our strategic sectors from non-standard market forces.

The main recipients of Chinese FDI are the “Big 3”: the UK, Germany and France. All of these countries already have a national FDI screening mechanism, which demonstrates that screening does not appear to dissuade foreign investments.

Despite not having national screening mechanisms for FDI, Chinese investments into the Central and Eastern Europe region remained modest, especially compared to Northern Europe and the “Big 3”. In addition, there have been many negative reactions to the Chinese FDI inflows into countries in this region. It can be noted that the reaction is rather triggered by speculative public debate than anything else.

All in all, it shows that Chinese investments do not give preference to systems lacking screening mechanisms, but quite the opposite.

China, Australia, Canada and US have screening mechanisms in place. In Europe, the initiative to have similar legislation came about at the national level. Therefore, the necessity to have an additional EU intervention in the process is at best doubtful.

**2. The regulation creates opportunities for political pressure, which affects the businesses’ decisions and MS sovereignty**

In Article 8 of the Regulation, setting the Cooperation Mechanism, it creates an obligation for Member States to inform the Commission and other MS of any FDI taking place in its territory. The Commission can then issue an opinion if it believes the given FDI may affect security or public order in one or more MS. If a different MS has reason to believe this FDI will affect its own security and public order, it can also issue an opinion. The text specifies later that the first MS should give “due consideration” to the

comments of the Commission and of the other MS. What “due consideration” entails, however, is not clear. The EP proposes adding that if one third of MS consider that the FDI is likely to affect their security and public order, the MS receiving investment should take “utmost account” of the comments. If those are not followed, the Commission shall “foster a dialogue” between the MS.

In its article 9, creating a screening framework for the Commission, the Regulation opens the possibility for the Commission to issue an opinion and request any additional information. If this opinion is not followed, the MS should draft a written explanation to the relevant parties (Commission and other MS).

Consequently, the Member States are not legally bound to follow the opinions. But neither Article 8, nor Article 9, explains what concretely happens if MS do not follow these opinions. It is not clear what is entailed by “fostering a dialogue” and what this written explanation should look like. It is not clear what happens if the other MS or the Commission do not agree with the explanation, do not consider it accurate or simply do not agree with the MS performing the screening.

Put differently, this **creates an opportunity** for the MS to **exercise political pressure**, throwing into doubt **the sovereign power to decide on the outcome of the FDI screening**. Legislators often tend to overlook the geographical structure of the markets. In the Machine Tool sector specifically, in order to produce any component, manufacturers order machine tools from different countries. **Value chains are global** and can be easily disrupted in conditions of uncertainty. Take as an example a company from MS A supplying to a manufacturing sector of MS B (such as aeronautics) with a component, such as landing gear. If MS A intended to sell this technology to a third country, MS B can oppose this decision, on grounds of security and public order. Involving several national political stakeholders can irreparably harm the business decision of an individual business actor.

### **3. The proposal needs a better-defined scope to avoid misinterpretations across MS.**

The definitions set out in Article 2, amended by the EP, are very broad. Any kind of investment, regardless of its size, can fall under the scope of the Regulation. The business decisions of small manufacturers and start-ups can be systematically undermined by the intervention of national governments and the Commission.

In the same way, the Commission or other Member States can request from the MS performing the screening any necessary information on planned or completed FDI to issue an opinion (Article 8). The EP has amended that the MS requests need to be made through the Commission and if the Commission or other MS have “justified reasons” for that. It is not explained, however, what justified reasons are, who decides whether the reasons are justified enough for the information to be given, and what happens if the information is not given or partially given. It is not clear what the course of action should be for Member States – if, for instance, they fear a threat to their security and public order – in the case of their request not being (fully) satisfied.

Furthermore, the lawmakers should give more guidance in the interpretation of security and public order. A reference to an EU definition should be given to avoid misinterpretations by member states and potential protectionism in FDI screening.

In parallel, efforts should be focused on achieving reciprocity in FDI flows between the EU and third countries through bi- and multilateral trade and investment agreements.

#### **4. Investment Screening Coordination Group and the risk of jeopardising confidentiality of sensitive information.**

The confidentiality of commercially-sensitive information is one of the main concerns for businesses in regard to this regulation. The Commission’s proposal superficially covers the confidentiality aspect in Article 11. The EP later adds provisions in Article 9 and 11 on handling such information with the “utmost attention” and “in compliance with Commission Decisions”.

Moreover, it introduces national FDI contact points, to be involved in the screening process and the implementation of the regulation. Institution-based contact points are expected to cooperate within the Investment Screening Coordination Group, bringing together experts and stakeholders from different Member States. CECIMO praises the intention to enhance cooperation between MS in FDI. However, the involvement of stakeholders – from local and national political authorities, the EC, trade associations, social partners, civil society – increases the risk of leaking crucial information to competitors. Having such a big and diverse group take a stand makes it difficult, if not impossible, to ensure confidentiality. In addition, if such information is leaked to the media, it might trigger unnecessary reactions in the public opinion, which creates additional pressure on national governments that might be reluctant to take an unpopular decision.

Although the regulation intends to create long-lasting and verified relationships with third-country investors, it might in fact deteriorate these relationships. If, in any way, this kind of information is leaked to the media, it would trigger public opinion on the topic – adding unnecessary political pressure on the decision-makers.

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