

THE EU FDI SCREENING REGULATION AND INTERNATIONAL INVESTMENT LAW: BETWEEN SOVEREIGNTY AND INVESTOR RIGHTS

REGULAMENTUL UE PRIVIND EXAMINAREA INVESTIȚIILOR STRĂINE DIRECTE ȘI DREPTUL INTERNAȚIONAL AL INVESTIȚIILOR: ÎNTRE SUVERANITATE ȘI DREPTURILE INVESTITORILOR

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Summary: *This article examines the European Union's evolving framework for screening foreign direct investment (FDI), focusing on the legal and institutional tensions between the EU FDI Screening Regulation (Regulation (EU) 2019/452) and international investment law (IIL). Introduced to address growing concerns over security risks posed by foreign—particularly state-backed—investments, the Regulation grants broad discretion to Member States while promoting a cooperative EU-level approach. However, this flexible structure has led to fragmentation, legal uncertainty, and inconsistent application across the internal market. The article analyzes the Regulation's procedural design, national discretion, and rationale for reform in light of recent institutional critiques. It further explores the compatibility of the EU screening regime with treaty-based investor protections, focusing on the scope of pre- and post-establishment rights, as well as the role of exclusion clauses, carve-outs, and security exceptions in limiting state liability. Ultimately, the article argues that while investment screening is a legitimate regulatory tool, its design and implementation must be carefully aligned with international legal obligations to preserve both strategic autonomy and legal predictability in the EU's investment landscape.*

Keywords: *Foreign Direct Investment (FDI); Regulation (EU) 2019/452; National Security; Public Order; Strategic Sovereignty/ Strategic Autonomy; International Investment Law (IIL); Screening Mechanism; Investment Protection Treaty/ International Investment Agreements (IIAs); Legal Fragmentation; Balance between Regulation and Investor Protection*

INTRODUCTION

Background

The screening of foreign investments has emerged as a defining feature of the EU's evolving trade and investment landscape, particularly during a period marked by geopolitical instability, economic fragmentation, and the growing strategic importance of national security¹. Regulation 2019/452, also known as the EU FDI Screening

¹ Regis Bismuth, 'Screening the Commission's Regulation Proposal Establishing a Framework for Screening FDI into the EU' [2018] *European Investment Law and Arbitration Review*, p. 47.

Regulation², was introduced to address growing concerns about foreign investments, particularly those with state-backed origins, targeting critical infrastructure, sensitive technologies, and other sectors deemed essential to public order and security. While the Regulation was initially framed as a neutral and protective measure, its timing and context suggested a direct response to the unprecedented wave of Chinese investments in Europe following the 2008 financial crisis, which reached its peak in 2016³.

Thus, the liberal attitude towards foreign investment that had long characterized EU internal market policy⁴ was tempered by a renewed emphasis on defensive instruments and the protection of strategic autonomy⁵. In practice, the Regulation established a cooperation mechanism among Member States and the Commission but left the actual screening decisions to the discretion of national authorities. While this approach introduced a structured EU-wide framework, it also created fragmentation, with diverse national procedures and criteria leading to uncertainty and inconsistency for foreign investors.

This shift in EU policy cannot be understood in isolation from broader international developments. Globally, the rise in screening mechanisms reflects a widespread concern that foreign direct investment (FDI), though traditionally a vital driver of economic growth, technological innovation, and global market integration, may also serve as a channel for strategic influence, economic coercion, and intellectual property theft⁶. As such, states have become more cautious, increasingly invoking national security and public order to justify interventionist measures⁷. These justifications, however, are often couched in broad and flexible terms, leading to legal ambiguity and potential overreach.

In the EU, the Commission has now proposed a revised FDI Screening Regulation aimed at strengthening coordination and expanding the scope of review, including retroactive scrutiny of completed investments and enhanced focus on indirect control by non-EU investors⁸. The proposal reflects a deeper shift in the EU's understanding of "economic public order," which now emphasizes resilience, technological sovereignty,

² Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union [2019] OJ L791/1 (FDI Regulation 2019).

³ Michelle Egan, 'Taking Back Control: The Political Economy of Investment Screening in the US and EU' in Elaine Fahey (eds.) *The Routledge Handbook of Transatlantic Relations* (1st ed, Routledge 2023), p. 206; after the financial crisis in 2008, Chinese investments reached an overall value of 37 billion euros in 2016, allowed into the Union without scrutiny.

⁴ Art 3(5) TFEU.

⁵ Xavier Groussot, Savvas Michael and Ema Mlynarcikova, 'The Screening of Foreign Investments in EU Law: When "Security and Public Order" Become the New Black in Internal Market Laws and Policies' (2024) 7(3) *Nordic Journal of European Law*.

⁶ Tania Voon and Dean Merriman, 'Incoming: How International Investment Law Constrains Foreign Investment Screening' (2023) 24 *Journal of World Investment & Trade* 75.

⁷ *Ibid.*

⁸ European Commission, Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) 2019/452 Establishing a Framework for the Screening of Foreign Direct Investments into the European Union, COM(2023) 329 final.

and the screening of investments based on potential long-term strategic dependencies⁹. While these objectives signal a more assertive economic governance, they may also be perceived as running counter to the liberal values underpinning the EU internal market and global trade integration¹⁰.

These developments increase potential conflicts with international investment law. While the EU assumes that investment screening is compatible with international obligations¹¹, from the perspective of the international investment law regime, the relationship is largely uncertain. In particular, scholars like Kilian Wagner¹², Jens Hillebrand Pohl¹³, and Tania Voon¹⁴, with Dean Merriman¹⁵, highlight tensions between the EU's FDI Screening Mechanism and international investment law (IIL). Wagner points out that while FDI screening allows states to protect national security through ex-ante scrutiny, it clashes with IIAs that offer ex-post protections like Fair and Equitable Treatment (FET) and non-discrimination, creating legal uncertainty. Pohl emphasizes that the EU's screening design reflects these treaty commitments by incorporating procedural safeguards to balance state sovereignty with IIA obligations; however, their application can still result in inconsistencies. Voon and Merriman further stress that IIL limits states' discretion, as overly broad or discriminatory screening risks violating investor protections. Together, they show that the EU's screening must carefully navigate between protecting critical interests and complying with international treaty obligations.

This article aims to fill the gap in the existing literature that lacks a detailed analysis assessing how the evolving EU framework falls within the scope of core IIA protections and what the limits of this protection are. As investment screening becomes a tool of broader economic and security policy, the risks of it becoming entangled with international obligations that were designed to constrain regulatory discretion are broader¹⁶. Understanding how the evolving EU framework for FDI screening interacts with its obligations under IIAs is therefore of pressing importance.

⁹ Hannah Ahamad Madatali with Lucia Torlai, 'Revision of the EU Foreign Direct Investment Screening Regulation' (2024) Briefing of the European Parliament, 22 July 2024, European Parliamentary Research Service (EPRS), <[https://www.europarl.europa.eu/RegData/etudes/BRIE/2024/762844/EPRS_BRI\(2024\)762844_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/BRIE/2024/762844/EPRS_BRI(2024)762844_EN.pdf)>.

¹⁰ Xavier Groussot, Savvas Michael and Ema Mlynarcikova, 'The Screening of Foreign Investments in EU Law: When "Security and Public Order" Become the New Black in Internal Market Laws and Policies' (2024) 7(3) Nordic Journal of European Law, pg 27.

¹¹ FDI Regulation 2019, Recital 5.

¹² Wagner K, 'Determining the Role of FDI Screening in International Investment Law' in Pohl JH et al (eds), *Weaponising Investments, Volume II* (Springer 2023) 116.

¹³ Pohl, J. H. (2020). The Impact of Investment Treaty Commitments on the Design and Operation of EU Investment Screening Mechanisms. In S. Hindelang, & A. Moberg (Eds.), *A Common European Law on Investment Screening (CELIS)* (pp. 725-768). Springer Nature Switzerland AG. https://doi.org/10.1007/16495_2020_5

¹⁴ Voon T and Merriman D, 'Incoming: How International Investment Law Constrains Foreign Investment Screening' (2023) 24 Journal of World Investment & Trade 75.

¹⁵ Ibid.

¹⁶ Kilian Wagner, 'Determining the Role of FDI Screening in International Investment Law' in Jens Hillebrand Pohl, Thomas Papadopoulos, Janosch Wiesenthal and Joanna Warchol (eds), *Weaponising Investments, Volume II* (Springer 2023), pg 116; Recital (3) and (35) FDI Screening Regulation.

Structure

This article adopts the doctrinal method as its central legal research approach. Following the introduction, Chapter 2 examines the Regulation's coordination mechanism, legal shortcomings, and rationale for amendment. Ch. 3 assesses compliance with IIA standards, focusing on the scope of treaty protections, especially during the pre-establishment and post-establishment phases. Ch. 4 analyses the substantive limitations to standards of treaty protection in the form of exceptions and exclusion clauses. The article concludes by reflecting on the EU's balancing of regulatory autonomy and investment protection.

EU FDI Screening Mechanism

Regulation (EU) 2019/452, adopted in March 2019 and fully effective from October 2020, represents a significant shift in the European Union's approach to foreign direct investment (FDI)¹⁷. While investment screening mechanisms have long existed at the Member State level, the introduction of this Regulation marks the first attempt to establish a coherent screening framework across the EU. Although the Regulation is relatively concise compared to other EU legislation or the proposed replacement, it lays out a comprehensive structure reflecting the EU's heightened emphasis on scrutinizing foreign investments. This development coincided with growing geopolitical tensions and increasing efforts to safeguard critical EU strategic interests.

Particularly, the Regulation aimed to respond to fears that some foreign investors might take control of EU companies that deal with important technologies, infrastructure, or sensitive information, which could affect security or public order across the EU. According to Article 1, the Regulation's main goal is to give Member States a way to screen investments that might pose risks to security or public order. Importantly, it recognizes that because the EU's internal market is highly integrated, an investment in one Member State can create risks that affect others, meaning security concerns are often transnational.

While not creating a single, unified EU-wide screening system, it sets minimum rules and encourages cooperation between Member States, by allowing each country to decide how and when to screen investments. This approach tries to balance the EU's principle of free movement of capital with the need to protect security and public order, supported by EU treaties, which leave national security mainly to Member States¹⁸. While this preserves Member States' control, it also leads to differences in how each country screens investments, making the system less predictable and more complicated for investors. This challenge is discussed further in this thesis.

The Regulation's attempt to balance security and free capital movement is complicated by the lack of clear definitions of "security" and "public order" in both the

¹⁷ European Commission, Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) 2019/452 Establishing a Framework for the Screening of Foreign Direct Investments into the European Union, COM(2023) 329 final.

¹⁸ Consolidated Version of the Treaty on European Union [2016] OJ C202/13, art 4(2); Consolidated Version of the Treaty on the Functioning of the European Union [2016] OJ C202/47, art 346

Regulation and EU law¹⁹. This vagueness gives Member States wide freedom to decide what counts as a security risk. While this allows flexibility, it also creates the risk that countries might use security concerns as a cover for protectionist or political goals. Although this discretion fits with the EU's principle of subsidiarity, it raises concerns about fairness, transparency, and legal certainty²⁰. Still, EU courts require that any restrictions on capital flows must be based on a real and serious threat and must respect the rules of proportionality and legal certainty²¹. This legal framework prevents Member States from abusing FDI screening to unfairly block investments.

The Regulation applies broadly to investments by legal or natural persons from non-EU countries that create lasting connections between the investor and a company in a Member State, especially when the investor gains some control or influence, usually understood as owning at least 10% of voting rights²². This wide scope shows the EU's intent to monitor many types of investments that could impact security or public order. However, as will later be illustrated, the lack of precise ownership thresholds adds to uncertainty in how the rules are applied.

This chapter explores the practical functioning of the Regulation by analyzing its operational structure and legal implications, with particular emphasis on the minimum standards required of national screening authorities. It also examines the cooperation and reporting duties shared between Member States and the European Commission, as well as the considerable discretion national authorities retain in setting and applying FDI screening criteria. The analysis highlights both the strengths and weaknesses of the existing framework, followed by a discussion on the rationale behind the planned amendments to the Regulation.

LEGAL FRAMEWORK FOR NATIONAL SCREENING MECHANISMS

Cooperation and reporting requirements

The most substantial part of the EU FDI Screening Regulation covers the rules that require Member States to share information with each other and with the European Commission. These cooperation and reporting duties are meant to make the process of reviewing foreign investments more coordinated and transparent across the EU. To better understand how this system works, it is useful to take a closer look at its main features.

Several articles in the Regulation set out how this information-sharing works. Article 3 requires Member States to inform the Commission when they set up or change

¹⁹ FDI Screening Regulation 2019, art 3.

²⁰ European Commission, Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) 2019/452 Establishing a Framework for the Screening of Foreign Direct Investments into the European Union, COM(2023) 329 final.

²¹ Case C-54/99 *Église de Scientology* [2000] ECR I-01335, para. 17.

²² FDI Screening Regulation 2019, art 2(1); see also Case C-446/04 *Test Claimants in the FII Group Litigation v Commissioners of Inland Revenue* [2006] ECR I-11753, para 181; Bas de Jong and Wolf Zwartkruis, 'The EU Regulation on Screening of Foreign Direct Investment: A Game Changer?' (2020) 31 *European Business Law Review* 447–474 p. 461.

their national screening systems. The Commission then passes this information on to the other Member States. Article 5 builds on this by requiring countries to send in a yearly report about the foreign investments they've received and how their screening rules have been applied. The Commission then uses this data to create a general report for the entire EU²³. This allows everyone to get a clearer picture of how foreign investments are being handled across the Union.

The Regulation also sets up a way for Member States to communicate during actual screening procedures. Article 6 states that when a country is screening an investment, it must notify both the Commission and the other Member States, including details about the investor and the investment. While it is not mandatory, the Regulation encourages the country doing the screening to list any other Member States that might also be affected²⁴. In addition, Article 7 allows any Member State to raise concerns about investments happening in another country, even if those investments haven't been screened yet. These concerns are also shared with the Commission, which can issue its own opinion that Member States need to give due consideration²⁵.

These rules are designed to help countries better understand whether an investment could affect not just one Member State, but possibly others too. This is especially important in a connected internal market like the EU, where investments can have cross-border impacts. If an investment may affect important EU projects or interests, the Commission can issue an official opinion that the Member State screening the investment must take seriously under Article 8(2).

However, this process can also cause delays and uncertainty for investors. The time needed to collect input from other countries and the Commission can slow down decision-making. Due to the lengthy procedure, in some cases, it may even open the door to reviewing an investment after it has already been made. This creates legal uncertainty and could potentially discourage investment, especially in sensitive areas like technology or infrastructure.

Even with these challenges, the Regulation has helped reduce the confusion and inconsistency that existed before. It brings more structure to how foreign investments are reviewed and encourages Member States to cooperate. But it doesn't go as far as creating one unified EU system. Instead, it leaves a lot of power in the hands of national governments²⁶.

This brings us to the Regulation's most debated parts, which allow each Member State to keep, change, or introduce its own screening system²⁷. This shows the EU's effort to find a middle ground: helping Member States work together while still letting them control their own national security decisions. However, this flexibility also means

²³ The Commission released its first mandated annual report on FDI screening in November 2021

²⁴ FDI Screening Regulation, art 6.

²⁵ Steffen Hindelang and Andreas Moberg, 'The Art of Casting Political Dissent in Law: The EU's Framework for the Screening of Foreign Direct Investment' [2020] 57 Common Market Law Review, p. 1435.

²⁶ FDI Screening Regulation 2019, Article 3(1).

²⁷ Ibid.

that the Regulation can still lead to uneven and unclear rules for investors. In the next part of this thesis, the focus will shift to what this national discretion means in practice and how it affects investor confidence, legal certainty, and the EU's broader goal of balancing openness with the protection of strategic interests.

Substantial Discretion of Member States

While the EU FDI Screening Regulation introduces key elements for coordinating investment review across the Union, a central characteristic of the framework is that the decision to establish a screening mechanism remains entirely within the discretion of each Member State²⁸. In other words, the Regulation does not impose an obligation to screen foreign investments; it merely allows for it and outlines how cooperation should occur if a Member State chooses to implement a screening process.

Thus, the Regulation does not contain binding rules or uniform standards. Instead, it offers examples of the kinds of sectors that may be sensitive to foreign control, such as critical infrastructure, advanced technologies, dual-use items, and entities dealing with sensitive information²⁹. This guidance serves as a flexible reference point, not a compulsory checklist. As a result, Member States retain considerable latitude in determining what constitutes a threat to national security or public order.

This flexibility, while preserving national sovereignty, has led to significant variations in how screening mechanisms are structured and applied across the EU³⁰. For instance, Member States differ in several respects: the level of foreign control or influence that triggers a screening process, whether the mechanisms are voluntary or mandatory, and whether the review occurs before (ex-ante) or after (post-establishment) the investment is made³¹. Some countries have adopted broad, cross-sectoral screening mechanisms that apply regardless of the industry involved, whereas others continue to focus narrowly on predefined sectors³². These differences contribute to a fragmented regulatory landscape that complicates investor expectations and increases legal uncertainty across borders.

Moreover, even where screening rules appear similar on paper, their application in practice can diverge significantly. This inconsistency is shaped by several factors. First, Member States do not necessarily have access to the same information³³. Even though the European Commission anticipated this risk of informational asymmetries and intro-

²⁸ Article 3(1) of the Regulation provides that "Member States may maintain, amend or adopt mechanisms to screen foreign direct investment".

²⁹ FDI Screening Regulation 2019, Article 4.

³⁰ European Commission, Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) 2019/452 Establishing a Framework for the Screening of Foreign Direct Investments into the European Union, COM(2023) 329 final.

³¹ Ibid.

³² Ibid.

³³ Bálint Kovács, 'Facilitating and Scrutinizing National Security Measures: Analysis of an Investment Screening Case in the European Union' in Janosch Wiesenthal (ed), *National Security and Investment Controls* (Springer Studies in Law & Geoeconomics, vol 3, Springer 2024) <https://doi.org/10.1007/978-3-031-68016-8>, pg 216.

duced provisions for sharing opinions and data among MS, their incorporation is still at the discretion of the MS conducting the review³⁴.

Second, MS are likely to interpret core concepts such as “national security” and “public order” differently, given the absence of precise definitions. These divergent interpretations could also be influenced by economic reasons. Economically weaker states may prioritize attracting investment, while more developed ones might adopt stricter controls, especially in strategic sectors. Additionally, disparities in industrial development, particularly in high-tech sectors, play a role³⁵. Less technologically advanced MS may welcome FDI as a way to catch up, whereas highly developed economies may prioritize protecting their strategic assets.

Scholars and commentators have voiced concern that the Regulation’s flexibility, especially as seen in Article 4, could invite unintended uses³⁶. As noted by de Kok, the lack of clear criteria undermines transparency, predictability, and legal certainty³⁷. This vagueness not only hinders meaningful judicial review but also deters litigation³⁸, given the procedural delays, limited chances of success, and possible reliance on confidential state information, to which investors may have restricted access. Ultimately, this risks fragmenting the internal market and eroding investor confidence, unless clearer rules and safeguards are introduced.

In summary, while the EU FDI Screening Regulation lays the groundwork for improved cooperation and risk awareness across Member States, it falls short of harmonizing screening practices. The wide discretion afforded to MS, combined with vague definitions and non-binding guidance, results in a patchwork of approaches that threaten legal clarity and investor confidence. Without stronger safeguards, clearer definitions, and more consistent application, the current regime risks being used not only to protect national security, but also – intentionally or not – as a tool for economic protectionism.

Rationale for Reform

Four years after the adoption of the Regulation (EU) 2019/452, concerns have only intensified regarding foreign, particularly state-owned, enterprises acquiring EU undertakings possessing critical technologies for strategic reasons³⁹. As a result, Member States

³⁴ Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union [2019] OJ L791/1 (FDI Regulation 2019).

³⁵ Bálint Kovács (n35).

³⁶ Naoise McDonagh, ‘Protection or Protectionism? Assessing the EU’s New Investment Screening Measures Against State-Driven Foreign Investment Risks’ (2021) 66(3) *The International Spectator* 108 <https://doi.org/10.1080/03932729.2021.1956182> ; Jochem de Kok, ‘Legal Remedies against Investment Screening Decisions’ in Bas de Jong et al (eds), *The Rise of Public Security Interests in Corporate Mergers and Acquisitions* (2022) 85.

³⁷ Jochem de Kok, ‘Legal Remedies against Investment Screening Decisions’ in Bas de Jong et al (eds), *The Rise of Public Security Interests in Corporate Mergers and Acquisitions* (2022) 85.

³⁸ Cheng Bian, ‘Foreign Direct Investment Screening and National Security: Reducing Regulatory Hurdles to Investors Through Induced Reciprocity’ [2021] 22 *Journal of World Investment and Trade*, p. 569.

³⁹ Xavier Groussot, Savvas Michael and Ema Mlynarcikova, ‘The Screening of Foreign Investments

have sought to preserve broad discretion in identifying sensitive sectors and defining national security concerns, as allowed under Articles 4(2) TEU and 346 TFEU. This has led to significant jurisdictional divergences and an increasingly fragmented legal landscape. In this context, an effective screening system must balance the need to prevent takeovers that threaten security or public order with the imperative to avoid discouraging desirable investments, particularly when transactions span multiple jurisdictions⁴⁰.

In December 2023, the European Court of Auditors (ECA) published its special report following a one-year audit of the FDI screening framework⁴¹, underscoring the consequences of such fragmentation. While the ECA acknowledged the Commission's efforts to implement the framework, it identified significant shortcomings in addressing security and public order risks. Notably, some Member States still lack national screening mechanisms altogether. The report highlighted that approximately 42% of FDI stock is located in such Member States⁴². Inconsistent definitions of critical sectors, variations in procedural safeguards, and differing interpretations of key terms create blind spots that weaken the EU's capacity to ensure coherent protection across the single market⁴³.

To address these issues, the ECA recommended several measures⁴⁴: clarifying key concepts within the Regulation, enhancing the quality of Commission recommendations and Member State reporting, improving the cooperation mechanism through the introduction of preliminary risk assessments for notified cases, and ensuring more rigorous oversight of national compliance.

Separately, the OECD, tasked by the Commission with evaluating the Regulation two years post-implementation, also found procedural inefficiencies⁴⁵. While transparency and cooperation had improved, problems such as delays, duplication, and rigid timelines often resulted in unsatisfactory outcomes for investors⁴⁶. While the framework showed signs of internal coherence, concerns about external coherence persisted, largely due to the evolving and inconsistent concept of national security. This legal uncertainty

in EU Law: When "Security and Public Order" Become the New Black in Internal Market Laws and Policies' (2024) 7(3) Nordic Journal of European Law.

⁴⁰ Ibid.

⁴¹ Ibid.

⁴² Ibid. European Court of Auditors, 'Special Report, Screening foreign direct investments in the EU – First steps taken, but significant limitations remain in addressing security and public-order risks effectively' (Publications Office of the European Union 2023) 5 <<https://www.eca.europa.eu/en/publications?ref=SR-2023-27>>

⁴³ European Commission, Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) 2019/452 Establishing a Framework for the Screening of Foreign Direct Investments into the European Union, COM(2023) 329 final.

⁴⁴ European Court of Auditors, 'Special Report, Screening foreign direct investments in the EU – First steps taken, but significant limitations remain in addressing security and public-order risks effectively' (Publications Office of the European Union 2023) 5 <<https://www.eca.europa.eu/en/publications?ref=SR-2023-27>>

⁴⁵ Stefano Riela, 'The EU's foreign direct investment screening mechanism two years after implementation' [2023] 22 European View, p. 64.

⁴⁶ OECD Report on the Framework for screening foreign direct investment into the EU. Assessing effectiveness and efficiency 2022 <<https://www.oecd.org/investment/investmentpolicy/oecd-eu-fdi-screening-assessment.pdf>>, p. 96.

has proven particularly problematic for non-EU investors engaged in multi-jurisdictional transactions. Additionally, the OECD observed a high volume of notifications in which investments were screened despite posing no real risk to public order or security, further illustrating the system's inefficiencies⁴⁷.

These institutional evaluations echo earlier scholarly concerns. Various authors have described the adoption of Regulation 2019/452 as “anything but uncontroversial,”⁴⁸ emphasizing the difficulty of reaching consensus on whether to screen, how to screen, and which authority should be responsible. Particularly, this peculiar framework produces inconsistency in the application of key criteria, such as who qualifies as a “foreign investor” and whether investments by EU-based entities controlled by non-EU investors must be screened. This limitation is particularly troubling in light of growing geopolitical tensions and the increasing use of complex corporate structures to mask the origin of capital⁴⁹. As emphasised by the Commission and Advocate General Ćapeta⁵⁰ in the 2023 *Xella* case, this limited definition of covered investments may fail to capture problematic indirect non-EU investments⁵¹.

Scope of Treaty Protection

Pre-establishment Phase

The applicability of international investment law to FDI screening measures before an investment is established largely depends on the specific language of the relevant IIA. Most IIAs traditionally limit substantive protections, such as National Treatment, Most-Favoured-Nation treatment, and Fair and Equitable Treatment, to investments that have already been made⁵².

An increasing number of international investment agreements, however, especially recent EU treaties concluded following the Lisbon Treaty, now provide protections extending to the pre-investment phase. Agreements such as the EU–Japan Economic

⁴⁷ European Commission, Evaluation of Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union accompanying the document Proposal for a Regulation on the screening of foreign investments in the Union and repealing Regulation (EU) 2019/452, SWD(2024) 23 final, 24 January 2024. <https://eur-lex.europa.eu/legalcontent/EN/TXT/PDF/?uri=CELEX:52024SC0023>, pg 36.

⁴⁸ Steffen Hindelang and Andreas Moberg, ‘The Art of Casting Political Dissent in Law: The EU’s Framework for Screening of Foreign Direct Investment’ (2020) 57(5) Common Market Law Review 1428.

⁴⁹ Ibid.

⁵⁰ Opinion of AG Ćapeta in Case C-106/22 *Xella Magyarország Építőanyagipari Kft* EU:C:2023:267, para. 53.

⁵¹ European Commission, Evaluation of Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union accompanying the document Proposal for a Regulation on the screening of foreign investments in the Union and repealing Regulation (EU) 2019/452, SWD(2024) 23 final, 24 January 2024. ; Case C-106/22 *Xella Magyarország Építőanyagipari Kft* EU:C:2023:568.

⁵² According to UNCTAD, 153 out of 2584 mapped treaties contain both NT and MFN provisions covering the pre-establishment phase.

Partnership Agreement⁵³ and the EU–Korea Free Trade Agreement⁵⁴ safeguard investors not only after investment but also during the establishment and acquisition stages, signaling a strategic EU move towards greater market access and liberalization. Likewise, treaties of certain EU Member States, including Finland-Kazakhstan BIT⁵⁵, similarly extend protections to the early phases of investment. For example, Article 3(2) of the Finland–Kazakhstan BIT applies MFN treatment to both “establishment” and “acquisition,” thereby encompassing pre-investment activities. Additionally, Article 1(3) defines an “investor” as an entity that invests in the territory of the other party in accordance with that party’s national laws and the treaty provisions, suggesting that prospective investors may benefit from treaty protections so long as their actions comply with domestic regulations and the terms of the agreement. It should also be noted that, although the EU has taken over external investment policy, the Finland-Kazakhstan BIT continues to apply and coexist with the EU’s external investment policies for the time being⁵⁶.

Moreover, despite not offering explicit pre-establishment rights, some treaties contain admission and promotion provisions that, in combination with the investment definition, may render substantive standards applicable. It was argued by Wagner⁵⁷ that clauses containing the obligation to grant FET “in every case”⁵⁸ or “at all times”⁵⁹ could suggest an extended application of the FET standard. This interpretation also finds support in arbitral case law. In *Nordzucker v Poland*⁶⁰, the tribunal had to apply a similarly worded admission and promotion provision of the Germany-Poland BIT⁶¹. The tribunal found that the phrase ‘in any case’ extends to investments in the making while excluding merely intended investments⁶².

Among the fourteen EU Member States that currently maintain FDI screening mechanisms, only a subset are parties to agreements that extend NT and MFN treatment

⁵³ Agreement between the European Union and Japan for an Economic Partnership, 17 July 2018 (not published in UNTS) OJ L330 of 27 December 2018, p. 3.

⁵⁴ Free Trade Agreement between the European Union and its Member States, of the one part, and the Republic of Korea, of the other part, 6 October 2010 (not published in UNTS) OJ L 127 of 14 May 2011, p. 6.

⁵⁵ Agreement between the Government of the Republic of Finland and the Government of the Republic of Kazakhstan on the Promotion and Mutual Protection of Investments, 9 January 2007, 2558 UNTS 585, art 1(1).

⁵⁶ Several German BITs contain this wording, e.g. Article 2(2) Admission and protection of investments German Model BIT available via <https://investmentpolicy.unctad.org/international-investment-agreements/model-agreements>.

⁵⁷ Kilian Wagner, ‘Determining the Role of FDI Screening in International Investment Law’ in Jens Hillebrand Pohl, Thomas Papadopoulos, Janosch Wiesenthal and Joanna Warchol (eds), *Weaponising Investments, Volume II* (Springer 2023), pg 132.

⁵⁸ German Model BIT, art 2(2).

⁵⁹ Art 2(2) (Promotion and Protection); Art 5(1) (Standard of Treatment) Slovakia Model BIT 2019 all available via <https://investmentpolicy.unctad.org/international-investment-agreements/model-agreements>

⁶⁰ *Nordzucker v. Poland*, First Partial Award (Jurisdiction), 10 December 2008; for a comprehensive analysis see: Marboe (2015), pp. 533 ff.

⁶¹ Germany-Poland BIT Article 2 (1), (signed 10 November 1989, entry into force 24 February 1991, terminated 18 October 2019)

⁶² *Nordzucker v. Poland*, First Partial Award (Jurisdiction), 10 December 2008, paras. 182–185.

to the pre-investment phase⁶³. Thus, although the application is limited, where such treaty provisions exist, tensions may arise between pre-establishment protections under IIAs and the EU's ex ante screening framework. Whether such claims are ultimately admissible or successful will depend on the specific language and structure of the applicable IIA, including any express exclusions or jurisdictional limitations within the treaty's dispute settlement mechanism.

Post-establishment Phase

As previously discussed, international investment agreements generally apply their standards of protection to the post-establishment phase. Consequently, although ex post screening is not expressly addressed in the EU FDI Screening Regulation (2019), its use under national legal systems typically brings such measures within the material scope of investment treaties, allowing investors to invoke the full range of protections afforded by these agreements.

Numerous treaties explicitly confine their coverage to established or “covered investments,” thereby excluding protections for the pre-investment period. For instance, the EU–Singapore⁶⁴ and EU–Vietnam Investment Protection Agreements⁶⁵ limit their safeguards to “covered investments,” effectively excluding activities before an investment is made. Similarly, Article 8.10(1) of the Comprehensive Economic and Trade Agreement (CETA)⁶⁶ restricts the application of FET, specifying “covered investments” and “investors with respect to their covered investments.” Such provisions clearly indicate that screening mechanisms applied prior to investment establishment fall outside the substantive obligations of these treaties and thus are generally not challengeable under international investment law.

Furthermore, what might initially be considered ex ante screening can, from a legal standpoint, be categorized as post-investment screening when it concerns expansions of already established investments⁶⁷. Even if the original investment was not subject to screening or was below the relevant thresholds, any later expansion subject to review is regarded as a post-establishment intervention. As highlighted by Pohl, the initial investment con-

⁶³ ee for example: Article 3(1) (Treatment of Investments) Finland-Armenia BIT (signed 5 October 2004, entry into force 20 April 2007); Agreement on the Promotion and Protection of Investments between the Italian Republic and Georgia (Italy–Georgia BIT) (signed 15 December 1999) art 2(2).

⁶⁴ Investment Protection Agreement between the European Union and its Member States, of the one part, and the Republic of Singapore, of the other part, 15 October 2018 (pending ratification) available at <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5714/download>, art 2.4.

⁶⁵ Investment Protection Agreement between the European Union and its Member States, of the one part, and the Socialist Republic of Viet Nam, of the other part, 30 June 2019 (pending ratification) available at <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5868/download>, art 2.5.

⁶⁶ Comprehensive Economic and Trade Agreement (CETA) between Canada, of the one part, and the European Union and its Member States, of the other part (signed 30 October 2016)

⁶⁷ Pohl, J. H. (2020). The Impact of Investment Treaty Commitments on the Design and Operation of EU Investment Screening Mechanisms. In S. Hindelang, & A. Moberg (Eds.), *A Common European Law on Investment Screening (CELIS)* (pp. 725-768). Springer Nature Switzerland AG. https://doi.org/10.1007/16495_2020_5

tinues to benefit from treaty protections regardless of whether subsequent expansions are scrutinized⁶⁸. Therefore, the implementation of FDI screening in such situations requires a careful balancing of the host State's regulatory interests and the investor's treaty rights.

Once a foreign investor has lawfully established an investment, any further screening of proposed expansions under mechanisms like the EU FDI Screening Regulation is classified as post-investment screening and must fully comply with treaty obligations. A host State's refusal to authorize such expansions does not invalidate the legality or protections of the original investment. Instead, any denial, conditional approval, or divestment order concerning expansions must conform to treaty standards⁶⁹. Should such measures undermine the investor's legitimate expectations or substantially reduce the investment's value, they may constitute violations of the FET standard or amount to indirect expropriation.

Given that treaty protections are fully applicable after an investment is established, claims brought during the post-establishment phase are generally more likely to succeed than those initiated in the pre-investment phase, where protections are often limited or expressly excluded. This firmer legal footing in the post-investment context amplifies the potential risks for host States when imposing restrictive screening measures on investments that have already been made.

Substantive Limitations of Investment Treaty Protections

Exclusion clauses

The applicability of investment treaty standards to investment screening mechanisms is heavily influenced by the presence of exceptions and exclusions within the treaty itself. One significant way that states limit the possibility of investor challenges to their screening measures is through the inclusion of carve-outs and reservations. Carve-outs, true to their name, are deliberate decisions made by treaty parties to exclude specific sectors from the treaty's obligations related to investment standards, including, in many cases, exclusion from the dispute settlement mechanism⁷⁰. Reservations differ in that they are unilateral measures by which certain sectors or measures, otherwise conflicting with investment standards and often labeled non-conforming measures, are explicitly excluded from treaty protection⁷¹. As a result, investors cannot invoke these measures to claim treaty violations.

Carve-outs and reservations are common tools used by states to narrow the scope of treaty application, particularly to restrict substantive standards or limit the reach of Investor-State Dispute Settlement (ISDS)⁷². This limitation typically targets entire policy domains or specific laws and regulations where states aim to retain full sovereign con-

⁶⁸ Ibid.

⁶⁹ Ibid; Voon and Merriman (2023), p. 113-114.

⁷⁰ Caroline Henckels, 'Should investment treaties contain public policy exceptions' [2018] 59 Boston College Law Review, p. 2828.

⁷¹ Joshua Paine, 'Global Telecom Holding v. Canada: Interpreting and Applying Reservations and Carve-Outs in Investment Treaties' [2021] 38 Journal of International Arbitration, p. 534.

⁷² Viñuales JE (2020) Seven ways of escaping a rule. In: Bartels L, Paddeu F (eds) Exceptions in international law. Oxford University Press, Oxford, pp 65–87.

trol. Examples include sensitive areas such as taxation, public procurement, or subsidies⁷³. Moreover, states frequently exclude whole sectors or industries from treaty protections. Investment agreements that offer pre-establishment protections often explicitly carve out sensitive sectors like telecommunications or energy, allowing states to protect critical national interests.

Several states have specifically used carve-outs and reservations to shield their domestic investment screening laws from treaty challenges⁷⁴. However, if investors can demonstrate that a carve-out was applied arbitrarily, discriminatorily, or with political motivation, tribunals may determine that residual treaty protections, such as non-discrimination or denial of justice, have been violated, even if the screening measure itself falls within the carve-out. Additionally, while more difficult, investors might sometimes invoke MFN clauses to circumvent reservations by claiming more favorable treatment available in other treaties⁷⁵.

While carve-outs generally provide states with effective defenses in arbitration when applied in good faith⁷⁶, they do not guarantee absolute protection from investor claims. This was demonstrated in the *Global Telecom v. Canada* case, where the investor challenged Canada's refusal to allow the conversion of non-voting shares into voting shares, a move aimed at gaining control in the telecommunications sector⁷⁷. Although the Canada–Egypt BIT contained a carve-out excluding arbitration over acquisition-related decisions, the tribunal adopted a narrow interpretation, ruling that share conversion did not qualify as an acquisition under international law, despite the treaty's broad definition⁷⁸. This case underscores that carve-outs may not fully shield states if tribunals interpret their scope restrictively.

Exception clauses

Treaty exceptions are common safeguards in international agreements, including BITs, that allow states to deviate from their obligations to protect national interests, especially in regulating investment screening mechanisms. These exceptions help balance the enforcement of investment standards with states' sovereign rights to regulate.

Exceptions are generally divided into general and security exceptions⁷⁹. General exceptions cover a wide range of public policy goals, such as protecting public morals, maintaining order, and conserving natural resources, and are modeled on similar WTO

⁷³ Ibid.

⁷⁴ Countries such as France, Italy, and Lithuania have lodged reservations specifically related to their domestic screening mechanisms; see also Article II(4)(b) of the Canada-Egypt BIT (signed 13 November 1996, entry into force 3 November 1997)

⁷⁵ David Collins, Introduction to Foreign Direct Investment: History, Trends and Rationales', in *An Introduction to International Investment Law* (2nd edn, Cambridge University Press 2020), p. 118.

⁷⁶ Kilian Wagner (n 39), p. 142.

⁷⁷ *Global Telecom Holding SAE v Canada*, Award and dissenting opinion, ICSID Case No ARB/16/16 IIC 1645 (2020).

⁷⁸ Ibid.

⁷⁹ Jens Pohl (n 49), p. 751.

provisions. Security exceptions, often inspired by Article XXI of GATT⁸⁰, allow states to derogate from treaty obligations to safeguard national security interests. Unlike carve-outs or reservations, which exclude treaty obligations upfront, exceptions permit states to implement otherwise treaty-infringing measures in specific circumstances.

Despite their importance, security exceptions face two main limitations: they are included in relatively few older treaties⁸¹ and are subject to varied and inconsistent interpretation by arbitral tribunals⁸². Early case law tended to strictly enforce nexus and self-judging requirements⁸³, while more recent decisions grant states wider discretion but impose limits on the legitimacy of security claims⁸⁴.

Moreover, the application of exceptions is constrained by conditions requiring that measures meet the clause's objectives, satisfy necessity tests, avoid arbitrariness or discrimination, and be exercised in good faith⁸⁵. These interpretative nuances create legal uncertainty and make it challenging for states to rely on exceptions to justify investment screening measures consistently.

CONCLUSION

The evolving landscape of foreign direct investment (FDI) screening in the European Union reflects a profound shift in the balance between economic openness and strategic autonomy. Regulation (EU) 2019/452 marked a critical step toward coordinating national screening efforts, yet it also exposed significant legal and institutional fragmentation. The Regulation's reliance on Member State discretion, absence of binding definitions, and broad scope of application contribute to a patchwork of national practices that undermine legal certainty and investor confidence across the internal market.

As the EU strengthens its screening regime – evidenced by proposals for reform and institutional reviews by the European Court of Auditors and the OECD – tensions with international investment agreements (IIAs) are becoming increasingly salient. The analysis shows that both pre- and post-establishment phases of investment may fall within the scope of treaty protections, depending on the treaty language and arbitral interpretations. At the same time, carve-outs, reservations, and exception clauses provide avenues for states to preserve regulatory space, though their effectiveness is constrained by legal standards such as non-discrimination, good faith, and proportionality.

⁸⁰ Article XXI of the General Agreement on Tariffs and Trade (GATT) 1867 UNTS 187.

⁸¹ According to UNCATD, 15% or 400 out of 2584 mapped treaties contain a security exception clause, see <https://investmentpolicy.unctad.org/international-investment-agreements/iaa-mapping>.

⁸² Burke-White W, von Staden A (2008) Investment protection in extraordinary times: the interpretation and application of non-precluded measures provisions in bilateral investment treaties. *Vanderbilt J Transnatl Law* 48(2):307–410

⁸³ *CMS v. Argentina*, Award, 12 May 2005, para. 359; *Enron v. Argentina*, Award, 22 May 2007, para. 332; *Sempra v. Argentina*, Award, 28 September 2007, para. 374.

⁸⁴ *CC/Devas v India*, Award on Jurisdiction and Merits, 25 July 2016, para. 245; *Deutsche Telekom v India*, Interim Award, 13 December 2017, para. 238.

⁸⁵ Andreas Ziegler and Jorun Baumgartner, 'Good faith as a general principle of International law' In Andrew Mitchell, M Sornarajah & Tania Voon (eds.) *Good faith and international economic law* (1st edn, Oxford University Press 2015), p. 18.

Ultimately, while the EU FDI Screening Regulation responds to legitimate security concerns, it must do so within the confines of international legal obligations. Ensuring consistency, transparency, and proportionality in screening practices is not only necessary for investor protection but also vital for maintaining the EU's credibility as a stable and rule-based investment destination. As the EU moves toward reform, a more harmonized and legally robust screening framework –aligned with international investment law – will be crucial to achieving both strategic resilience and legal predictability in the global investment environment.

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