U.S. Multinational Direct Investment: Regulation by Member States of the European Community

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NOTES

U.S. MULTINATIONAL DIRECT INVESTMENT: REGULATION
BY MEMBER STATES OF THE EUROPEAN COMMUNITY

I. Introduction

Direct investment, as opposed to portfolio investment, involves investment by U.S. companies in overseas branches, subsidiaries, and associates, as well as acquisition of controlling interests in existing foreign companies. This method of foreign investment includes both the transfer of money capital by the U.S. company to the foreign market, and the transfer of management and technical guidance, dissemination of technical knowledge through the establishment of foreign research and development departments, and the dissemination of production and marketing skills. The principal advantage of direct investment to the U.S. company is that it enables the U.S. company to maintain substantial control over the management of its foreign investment. The major economic decisions regarding the development of the investment opportunity are made by decision-makers residing outside of the host country.

This aspect of foreign direct investment has caused European host countries, particularly France, to rebel against the growing input of foreign direct investment. The current prevalence of direct investment by U.S. companies in Western Europe has led countries such as France to warn other European countries that their economies are subject to the control of outsiders. This warning has not, however, led other European countries to prevent U.S. companies from continuing their direct investment.

The U.S. based multinational companies have steadily increased their direct investment in Western Europe since 1950. The major factor contributing to this increase was the formation of the European Economic Community (E.E.C.). The Treaty of Rome which created the E.E.C. was signed in 1957 and ratified in 1958 by West Germany, France, Italy, the Netherlands, Belgium, and Luxembourg. The formation of the E.E.C. created a continent-size market, with demographic and economic characteristics similar to that of the United States, in which U.S. multinational corporations (MNCs) could establish and operate efficiently and effectively.

The announced purpose of the Treaty of Rome was to create a European Economic Community through:

(a) the progressive reduction and removal of all fiscal and physical restrictions on the free movement of goods, capital, and persons among member states,
(b) harmonization of their economic policies, and

1 Portfolio investment is the acquisition of stocks and other securities of a business concern which is located in a foreign country. It does not include any accompanying control over or participation in the management of a foreign concern.
2 P. COLEBROOK, GOING INTERNATIONAL 4 (1972).
3 The U.S. Department of Commerce's Survey of Current Business (1974) shows that in 1950 U.S. direct investment in Western Europe was $1.7 billion, in 1960 it was $6.7 billion, and by 1974 it had grown to $44.5 billion.
These three goals have encouraged U. S. direct investment in the E.E.C. by disadvantaging American industrials attempting to penetrate the European Common Market as "outsiders" via exports from their plants in the U. S. and other non-Common Market countries. First, the member states of the E.E.C. developed a Common External Tariff (C.E.T.). The C.E.T. imposes tariffs against products being imported into the E.E.C. from non-member countries; these tariffs are not applicable to the same products if they are produced in one of the E.E.C. member states. Goods manufactured by a company in the U. S. formerly could compete with Italian goods in a French market, for example, because both goods were subject to the same French tariff. Under the C.E.T., however, the American product is subject to the Common External Tariff, whereas the Italian product will enter the French market tariff-free. Consequently, goods manufactured in the U. S. are now at a competitive disadvantage with goods produced within the E.E.C. The only way a U. S. company is able to overcome this tariff discrimination is to establish a production operation in an E.E.C. member state. Because the product will now be produced within the E.E.C., it will escape the C.E.T.

Second, the E.E.C. treaty provisions concerning the elimination of all restrictions on the free movement of goods, persons, and capital among member states apply to all companies and persons duly established within a member state pursuant to Article 58 of the E.E.C. Treaty, regardless of their nationality or the nationality of their owners. Due to the fact that capital markets in the E.E.C. member states have been substantially broadened because of the removal of restrictions imposed on the shifting of capital from one member state to another, U. S. subsidiaries now have a substantially broadened pool of capital from which they are able to draw the funds necessary to finance their operations.

Further, the E.E.C. Treaty permits companies, including U. S. subsidiaries, established in one member state to establish operations within the territory of any other member state. This presents an unusual advantage to an American company seeking to establish a subsidiary in one of the member states.

A further advantage to an American company occurs due to the failure of the E.E.C. to achieve its third goal, the harmonization of the member states' economic policies, as this has enabled American companies to use the divergent economic and commercial policies of the different member states to gain pref-

4 In 1962, the Member States adopted a Common External Tariff (CET) to be applied by all Member States to all imports coming from areas outside of the E.E.C. Moreover, the Member States achieved a system of tariff-free internal trade in 1968. Harmonization of the economic policies of the Member States, as provided for by Articles 110-113 of the Treaty of Rome, however, has been predictably slow.

5 The term "outsiders" refers to a company which does not have a production unit or other direct investment established in one of the Member States of the E.E.C.

6 L. Krause, European Economic Integration and the U.S. 120 (1968).

7 See Treaty of Rome, arts. 9, 48, 67.


9 Krause, supra note 6, at 120.
erential positions within the E.E.C. This note will outline the present regulations in France and the United Kingdom as examples of divergent policies within the E.E.C.

These three factors have encouraged American MNC's to establish direct investments within the European Common Market. The usual procedure followed by a U. S. MNC is to apply for permission for the proposed direct investment directly to the host country government. If permission is granted the corporation need only comply with the host country's direct investment and exchange control regulations. If, on the other hand, the requested permission for establishment of the proposed direct investment is refused or granted only on terms which are discriminatory against the American company, the company need not capitulate. Two alternatives are available to the American company. It can take advantage of the failure of the E.E.C. to formulate a common commercial policy by informing the host government that should it refuse to give permission for the proposed direct investment, the direct investment along with all of its economic benefits will be established in one of the other E.E.C. member states.

If the company's attempt to use its economic leverage to gain the desired permission for the proposed direct investment fails or if the company is too small to possess a sufficient amount of economic leverage, it can take advantage of the right of establishment provisions of the E.E.C. Treaty to gain the desired permission. In order to invoke the right of establishment the American corporation must first satisfy the conditions stipulated in Article 58 of the E.E.C. Treaty. Satisfaction of these requirements will entitle the U. S. company "to be treated in the same way as natural persons who are nationals of member states." Once the U. S. corporation has qualified as a national of a member state it will be able to enjoy the benefits of Articles 52-57 of the E.E.C. Treaty, which guarantee to nationals of member states the right of establishment anywhere within the E.E.C. By use of these treaty provisions the U. S. company may gain access to that host country which had previously refused to grant permission for the proposed direct investment.

II. Nationalism: A Force Stronger Than Economic Integration

A. The Problem

One of the objectives of the European Economic Community is to develop a common commercial policy to facilitate the economic development of Western Europe. The E.E.C., as a unified community, has not been successful in developing the common commercial policy envisioned by the Treaty of Rome. Progress toward this goal has not extended beyond the stage of Committee reports. Various reports have been submitted to the European Commission outlining the problem and stressing the need for the formulation of a common economic or social policy. One of the most significant reports is the Colonna
Report,\textsuperscript{13} which emphasized the strengthening of European business enterprises in conjunction with the formulation of a common industrial policy to promote these European enterprises. The report was especially concerned with the high technology sectors of industry, which are the sectors in which U. S. multinational competition is the strongest. Several other reports have also urged the necessity for the unification of member state commercial policies toward non-member countries to prevent multinational companies from non-member countries from gaining competitively advantageous positions within the E.E.C.\textsuperscript{14}

To date, no common commercial policy has been acceptable to all member states. Each member state, therefore, continues to formulate its own commercial policy to regulate the type and quantity of foreign direct investment it will permit within its borders.

The causes of this difficulty in formulating a common commercial policy among the E.E.C. member states are many. The primary reason is that each member state finds it difficult to relinquish significant control over the management of fundamental domestic commercial and economic policies. The member states fear that a transfer of control over their fundamental economic policies to the centralized institutions of the E.E.C. would involve a sacrifice of sovereignty. This is a step which these governments, particularly France, are not willing to take. The fear is that the decision-makers of the institutions, being from a community perspective, will fail to adequately consider the impact on the individual member states.

The national governments of the member states are also experiencing an increase in pressure from their citizens to assume greater responsibility for the economic and social welfare of their nationals.\textsuperscript{15} Furthermore, these governments have been grappling with unfavorable balance of payments problems, high inflation, and currency devaluation. Faced with these immediate and grave problems the member states have been compelled to choose between concentration on their own domestic policies or concentration on their commitment to further economic integration and non-restrictive trade within the E.E.C.\textsuperscript{16}

The member states have tried, unsuccessfully, to strike a balance between these two alternatives. At present, domestic pressures and the ever-present force of nationalism have led to a commitment to local concerns. Consequently, there exists among the member states of the E.E.C. a lack of international obligation.\textsuperscript{17} The industrial, commercial, and economic policies in the E.E.C., therefore, remains the prerogative of the individual member states despite the underlying objective of E.E.C. membership, the development of common commercial policies to facilitate the economic growth and development of Western Europe.

B. Consequences of Nationalism and a Possible Solution to the Rising Tide of U. S. Multinational Corporations

The strategic planning in a multinational company is carried out by the

\textsuperscript{13} The report was submitted to the European Commission in the summer of 1971.
\textsuperscript{14} C.E.D., supra note 8, at 21.
\textsuperscript{15} CAIRNCROSS, et al., ECONOMIC POLICY FOR THE EUROPEAN COMMUNITY 116 (1975).
\textsuperscript{16} Id.
\textsuperscript{17} Id. at 117.
top management at the parent company located in the home country of the multinational corporation. Such planning consists of the formulation of overall corporate objectives, policies, and strategies. The local subsidiaries, in turn, will formulate their own objectives, policies, and strategies consistent with those outlined by top management. The effect of this planning hierarchy is to place the overall economic decision-making of local subsidiaries, based in member states, in the hands of the corporate headquarters located outside the E.E.C. This system of decision-making promotes the interests of the multinational company without consideration of the significant impact these decisions may have on the economic welfare of the host country. The host countries fear that all of this power, concentrated in the hands of multinational corporations, may weaken or even destroy the effectiveness of host government’s economic policies.

An incident which occurred in 1976 in the United Kingdom illustrates this problem. Chrysler, U.K. had been operating at a loss for the past several years. The primary reason for this deficit was the labor unrest. The Chrysler, U.K. subsidiary, therefore, was putting a heavy drag on overall corporate profitability. In the winter of 1975-1976, the President of Chrysler Corporation in the United States decided to close out the U.K. subsidiary. Doubting the possibility of a sale, he suggested that Chrysler simply give the plants to the British government.

The impact of such a decision for Chrysler would have been to improve the corporation’s worldwide profitability. The impact for the British economy would have been devastating. Their economy was presently encountering high inflation, currency devaluation, high welfare payments, and high unemployment. The shutdown of Chrysler’s two large plants would have forced thousands of laborers into the swelling ranks of the unemployed. It would have forced the British Government to operate the two plants; the government was already experiencing difficulty managing British Leyland, the coal and steel industries, and the railroads.

The only alternative available to the British Government was to convince Chrysler not to pull out of the U.K. by giving it an economic incentive to remain. The government chose to exercise this option. The incentive took the form of government subsidies which were guaranteed to Chrysler to make up any losses they suffered from their U.K. subsidiary.

Incidents such as this have alarmed host governments around the world. They fear what might happen in their own countries as large multinational corporations continue to dominate large sectors of their economies. Consequently, many governments are taking a harder line toward the multinational corporations. In the E.E.C. France is the leader in such a crusade against the free expansion of multinational corporations, especially those of American origin. It has become evident, however, that the only viable means for France or any other member state to effectively control the expansion of multinational corporations is through the adoption of a common commercial policy.

European leaders have been slow to do much toward the accomplishment

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19 C.E.D., supra note 8, at 36.
of the goal of a federalized Europe. France impaired the progress in 1969 when the Luxembourg Accords were signed by the original six member states, at the insistence of France. The Accords reestablished the veto power of each member state in regard to matters of national importance. Consequently, if a single member state refuses to adopt a policy agreed to by all other member states, provided it is an area of national importance, then the policy will not be enacted. Nationalism continues its reign and the European Common Market has failed to progress beyond a customs union. No common economic or commercial policy has been established. Regulation of foreign direct investment remains a national concern.

Another unrealized goal of the E.E.C. is the unification of the company law of the member states. The Commission has recognized that it is vital for industrial concentration to occur on a Europeanwide basis in order to facilitate the development of technology. To form European companies, the fiscal and legal barriers to close relations and mergers between companies of different member states must be removed by the E.E.C. The removal of these barriers would be facilitated by the adoption of a European Company Law. Divergences in the various national company laws and corporate tax laws have discouraged the establishment, transfer, and merging of companies. The head office of a company cannot be transferred from one member state to another without changing its judicial status. Most of the mergers which occurred following the formation of the E.E.C., therefore, have occurred between business concerns of the same member state.

To carry out its objective of creating European companies, the Commission must harmonize European Company Law. In this regard, the Commission has proposed a number of company law directives. These proposals have exerted considerable influence on the national legislatures of the member states. The member states have used these proposals as models for reforming their own company law. As this process continues, the traditional barriers to transnational mergers, due to the vastly divergent national company laws, will be removed. It will also become easier for the national legislatures to agree to adopt Community measures on company law in the future.

There are three primary political problems, however, confronting the success of a community effort to develop an E.E.C. company law. One problem involves the conflict as to whether there should be worker representation on the supervisory board of a European Company. The Commission proposals and several member states favor a two tier board system; the Board of Directors, which is elected by the shareholders, and the Supervisory Board, which is elected

20 CAINRCROSS, supra note 15, at 131.
21 Id. at 132.
22 In France, for example, the Institut de Developpement Industriel was set up in 1970 by the French government to encourage concentration of most of France's largest industrials. Sud-Aviation, Nord-Aviation, and SEREB have been merged. A government reorganization of the electronic and chemical industries has also been completed. The U.K. government created the Industrial Reorganization Corporation. It was given the finances in 1967 necessary to bring about the merger of three U.K. computer companies to form International Computers, Ltd. (ICL).
by the employees. A second problem involves the difficulty in determining what should be the tax status of a European Company. Finally, there is a problem as to which companies should be allowed access to European incorporation.\textsuperscript{24} The proposed statute requires the company to have a certain size, a certain minimum capital, fully paid in, and it must be incorporated in at least two different member states.

Until such problems are resolved and the member states can overcome their nationalism, the potential for a political and economic union of the E.E.C. will remain only an illusion. The concept of a European enterprise incorporated under a European company law to combat U.S. multinational corporations will remain an impossibility. The "American Challenge" will have to continue to be confronted on a national level through a system of national regulations and business incentives similar to those currently enforced in the U.K. and France. The foreign multinational corporations will continue to be able to exploit the large market created by the E.E.C. American companies will be able to use the divergent national economic policies of the member states to their best advantage.\textsuperscript{25}

Because American companies planning to extend their operations into the European Common Market must conform to national policies and regulations of the host country, an examination of the British and French regulations will provide an example of what a corporation making a foreign investment in those countries should expect.

III. Regulation of Foreign Direct Investment on a National Level: The British and French Experiences

A. Introduction

National policies on taxation, foreign exchange controls, foreign investment incentives, and competition are only a few areas in which the policies differ widely among member states of the E.E.C.\textsuperscript{26} As will be explained below, multinational corporations can exploit these variations in national policies to their benefit and to the disadvantage of the particular member states involved. It is important, therefore, for any American firm planning a direct investment in the E.E.C. to evaluate the applicable national restrictions and regulations on direct investments.

If the investment proposal involves a high technology industry such as shipping, communications, banking, or the public utilities, special prohibitions are likely to be applied by the host governments, because these industries are


\textsuperscript{25} Economic integration does mean that each Member State will lose some control over its domestic economic welfare. It will gain, on the other hand, some control over the economic welfare of the other Member States. If they would understand this give-and-take relationship involved in economic integration, they would understand that their fear concerning the loss of economic sovereignty has been unfounded or, at least, overemphasized.

\textsuperscript{26} Cairncross, \textit{supra} note 15, at 138.
held to be vital to national interests.\textsuperscript{27} Also, a direct investment which contemplates the acquisition of an existing domestic enterprise by an American company would be met with favor in some E.E.C. countries, such as the United Kingdom, and with resistance in other E.E.C. countries, e.g., France.\textsuperscript{28}

The French Government prefers to have the acquisition of an existing French enterprise undertaken by another French enterprise. Consequently, French law permits a domestic competitor to intervene in the attempted acquisition of a French company by a non-French company. The Ministry of Finance will inquire as to whether another French company is willing and able to acquire or merge with the French enterprise under consideration. If such a French alternative is available the Ministry of Finance may refuse to give authorization for the proposed acquisition to the American company.\textsuperscript{29}

Another item of confusion involving acquisitions is the fact that what the American company believes to be a mere portfolio investment may be held to be a direct investment under the law of the host country. When the sum of capital involved is larger than a stated maximum for portfolio investment, or when the market shares of the buyer and seller exceed a particular percentage of the total, the investment will be regarded by the member state as a direct investment and will be subjected to the direct investment regulations rather than to the portfolio investment regulations. The maximum amount allowed for portfolio investment differs among the member states.

Consequently, when an American company contemplates undertaking a direct investment in the E.E.C. it is essential for that company to analyze the various alternatives available to it. It should analyze the investment regulations and incentives applicable to the proposed investment in each member state. The investment should be undertaken in the country offering the most favorable treatment for the investment. It should be noted, however, that if the U.S. company must make the investment, for business reasons, in a particular member state whose treatment of the investment would be discriminatory against the American company, it may be able to overcome this discrimination by one of the methods explained below.\textsuperscript{30}

The investment regulations and incentives imposed by the United Kingdom and France illustrate the diversity which exists within the Common Market community. The U.K. has been traditionally receptive to American direct investments, while France has been traditionally more protective of its domestic industry, more nationalistic in its attitude, and more hostile toward foreign direct investment, particularly that from the United States. An American company must be aware of these national philosophies and adjust its approach to a direct investment project in such a way as to put the host government at ease.

B. American Direct Investment in the United Kingdom

1. Foreign Direct Investment Favored

\textsuperscript{28} \textit{Id.}
\textsuperscript{29} \textit{See text accompanying note 90 infra.}
\textsuperscript{30} \textit{See Part IV infra.}
The United Kingdom is one of the largest recipients of American direct investment. Approximately 85% of foreign direct investment into the U.K. is of American origin.\textsuperscript{31} The U.K. was the recipient of over 10% of American worldwide direct investment in 1973.\textsuperscript{32}

The U.K. has favored foreign direct investment, especially from the U.S.A., for two major reasons. The U.K. is primarily an exporter of finished goods. The goods produced for export by the U.S. subsidiaries located in the U.K. make a positive contribution to the U.K. balance of trade. In 1972, for example, U.S. subsidiaries produced over 17% of the total U.K. exports.\textsuperscript{33} Moreover, foreign direct investment is favored because many U.K. business firms are multinational corporations and think in terms of world markets rather than in terms of national markets. In contrast, most European companies on the continent think solely in terms of domestic markets. Few of these companies are true multinational corporations. The continental businesses view the rising influx of U.S. direct investment as an attempt by American companies to dominate the Western European economy. The U.K., on the other hand, views U.S. multinational company direct investments, not as an attempt to dominate the European economy, but as an attempt to maintain its share of the world market.\textsuperscript{34}

Over the past several years, however, even British enthusiasm for U.S. company subsidiaries has dwindled because U.S. parent companies tend to take up 100% ownership of their foreign operations and maintain tight control over the financial and economic affairs of these subsidiaries.\textsuperscript{35} Such control has generated concern on the part of the British Government because of the presumed effect that this external control has on the economic and political sovereignty of the U.K.\textsuperscript{36} Foreign control over these subsidiaries creates, at least, a potential

\begin{table}[h]
\centering
\begin{tabular}{|c|c|c|c|c|}
\hline
\textbf{year} & \textbf{World} & \textbf{U.K.} & \textbf{E.E.C.} \\
\hline
1965 & 49.5 & 20.6 & 6.3 & \\
1966 & 54.8 & 10.7 & 5.1 & \\
1967 & 59.5 & 8.6 & 6.1 & 7.6 & 20.6 & \\
1968 & 65.0 & 9.2 & 6.7 & 9.0 & 7.1 & \\
1969 & 71.5 & 9.2 & 7.2 & 10.3 & 14.4 & \\
1970 & 78.2 & 10.1 & 8.0 & 11.8 & 14.5 & \\
1971 & 86.2 & 10.2 & 9.0 & 12.5 & 15.3 & \\
1972 & 94.3 & 9.4 & 9.6 & 13.6 & 15.4 & \\
1973 & 107.3 & 13.7 & 11.1 & 15.7 & 22.9 & \\
1974 & 118.6 & 12.0 & 12.5 & 10.0 & 21.7 & 18.5 & \\
\hline
\end{tabular}
\caption{U.S. Direct Investment (Book value— all industries, $ billions)}
\end{table}

31 M. Steuer, P. Abell, J. Gennard, M. Perlman, R. Rees, B. Scott, & K. Wallis, \textit{The Impact of Foreign Investment on the United Kingdom} ¶ 5-10 (1973) [hereinafter cited as \textit{Steuer}].

32 The following table, prepared by the U.S. Department of Commerce, \textit{Survey of Current Business} (1974), shows the percent of total U.S. direct investment in the U.K. and in the original six E.E.C. countries between 1965 and 1974:


36 Lincoln, \textit{supra} note 33, at 8.
shift of some decision-making to outside the host country. The parent company located in the United States may direct the local subsidiary to produce a certain product, lay off a certain number of employees, or make other decisions of a financial or economic nature. These decisions are being made in satisfaction of the best interests of the parent company irrespective of the economic welfare of the U.K. As a result of this perceived threat to British autonomy, foreign direct investment is becoming subject to closer scrutiny.

2. The U.K. Is a Favored Host Country of U.S. Multinational Corporations

The policy employed by the host country is a major determinant of whether a U.S. company will invest in that country. The attitude with which the host country government perceives the economic, social, and political affects of foreign direct investment influences the choices of potential investors. Part of the reason for the U.K.'s popularity among American corporations is, therefore, that the U.K. generally perceives foreign direct investment as having a net beneficial effect. The new technology, management skills, tax revenue, labor training, and contribution to the U.K. balance of trade outweigh any negative effects which may be associated with the direct investment. As will be seen, France, on the other hand, perceives foreign direct investment as a serious threat to its national sovereignty, economic welfare, and the survival and growth of domestic industry. Therefore, France maintains a very restrictive attitude toward foreign direct investment.

Aside from its favorable policy, American multinational corporations favor the U.K. as a host country because the U.K. provides a tariff-free springboard to the large markets in the E.E.C. and the Commonwealth. The U.K. also offers to the U.S. multinational corporation a large skilled labor force with a common language and heritage. Further, the U.K. labor force has the lowest wage rate of all the E.E.C. countries.

A fourth factor operating to enhance the attractiveness of investment in Britain concerns the fact that the U.K. has been politically stable. There has been a general respect for the rule of law, and no nationalization of foreign corporations. There also have been fewer post-war governments than in either France or Italy. The bureaucracy involved in the procedure provided for obtaining permission to make the investment is relatively small. London provides easy access to the Eurodollar market, because it is the financial center of Europe, and repatriation of profit presents little difficulty. Finally, the average rate of return on U.S. direct investment in the U.K. has been appreciably superior to that in the original six E.E.C. countries.

3. Investment Regulations

The Exchange Control Act of 1947, as amended in July, 1973 and De-

37 Foreign Investment in Britain, [1976] 1 Doing Business in Europe (CCH) ¶ 23,651.
38 In 1970, for example, the hourly wage rate in the U.K. was 40% of the U.S. hourly wage rate for comparable jobs.
39 Lincoln, supra note 33, at 19.
40 In 1971 the return on U.S. direct investment was 10.9% in the U.K. and 6.3% in the original six E.E.C. countries. See Lincoln, supra note 33, at 23 passim.
cember, 1974, under the section entitled Inward Direct Investment, sets forth the general policy of the U.K.: "The general policy of Her Majesty's Government is to welcome direct investment in the U.K. by non-residents provided it is appropriately financed." If an investing company is not certain that it has the appropriate financing, it may make an application to the Bank of England for a comment on whether its proposed financing procedure is acceptable or requires modification. Exchange control permission must be acquired not only for all investment by persons not resident in the Scheduled Territories, but also for those investments by persons, regardless of where they are resident, which involves, directly or indirectly, the loss of control by U.K. residents of existing U.K. companies.

The U.K. Government will consider on a case-by-case basis those proposals involving the take-over by nonresidents of existing U.K. companies which by their size or nature constitute a vital part of British industry. Furthermore, the Bank of England requires that all applicable requirement of the City Panel on Take-Overs and Mergers are met. If the foreign direct investment involves amounts less than £50,000, and no special national interests are involved, then the Bank of England has the authority to grant or deny permission for the investment. In all other cases, approval is required from the Treasury, which acts in consultation with the Department of Trade and Industry.

The Exchange Control Act normally requires that the financing of the investment be either in sterling from an external account or in currency. Once the fixed assets have been appropriately financed, however, the subsidiary of a foreign company will normally be given free access to sterling borrowing within the U.K. for working capital purposes. These regulations are not applicable to companies or residents of other E.E.C. countries and those companies not indirectly owned by residents of non-sterling third countries. Such companies may borrow sterling in the U.K. without limit for direct investment purposes in the U.K. This discrimination in favor of E.E.C. established companies is required by the E.E.C. Treaty and directives on capital movements.

41 Inward direct investment is defined by the Exchange Control Act of 1947, as amended, to include: "those investments in which the investor establishes, expands, or consolidates an economic enterprise with the intention of participating in its management and operation; and trade investments where the investor establishes or maintains commercial links with other companies to further his existing business."


43 "Scheduled Territories" is defined in the Exchange Control Act of 1947 as those territories comprising the U.K. including the Channel Islands, the Isle of Man, the Republic of Ireland, and Gibraltar.


45 Id.


47 Id.

48 Sterling from an external account refers to any sterling which the foreign investor is able to acquire outside of the U.K.

49 An exception to this general rule exists when there is an establishment of a new plant in a development area. In such a case financing within the U.K. is permitted.

50 STEUER, supra note 31, at ¶ 9.10, 9.11.

51 Article 67 of the Treaty of Rome states: "During the transitional period and to the extent necessary to ensure the proper functioning of the Common Market, Member States shall progressively abolish between themselves all restrictions on the movement of capital belonging to persons resident in Member States and any discrimination based on nationality or on the
When foreign direct investment involves the take-over, by nonresidents, of existing U.K. companies, the Department of Trade and Industry will examine the general desirability of the proposed take-over. The Department of Trade and Industry determines if the proposed take-over satisfies the following criteria established as guidelines for acceptable take-overs:  

1. The investment must make an ‘appropriate’ contribution to foreign exchange reserves.

The term “appropriate contribution” means that the amount of foreign capital brought into the U.K. to finance the fixed assets of the company must be proportionate to the interest which the foreign company has in the subsidiary.

2. The price given as consideration must be a fair one. It must reflect the fair market value of the assets acquired by the foreign enterprise.

3. Any further financing of fixed assets must be provided from sources outside the U.K., at least, in proportion to the amount of interest acquired by the foreign firm.

Whenever a foreign investor makes a share purchase in the market which would give the investor a 10% control of the equity of a U.K. company, the general permission for market purchases does not apply and the investor must obtain the specific permission of the Bank of England before purchase of the shares can be made. Moreover, regardless of the percentage of control involved, if the foreign investor intends to participate in the management or operation of the company whose shares are so acquired, the rules for inward direct investment must be complied with, not the rules for inward portfolio investment. The investor who wishes only to be subject to the rules for a portfolio investment must not acquire enough shares to give him a 10% control of the firm.

If the investment gives the investor a 10% control of the British enterprise, this percentage of ownership is deemed to be sufficient to give the investor a significant voice in the management of the enterprise. The British Government therefore requires that a purchase of shares involving 10% control of the equity be treated as a direct investment. The investor should make clear his intention to the U.K. that he is acquiring the shares solely as a financial investment and with no intention of participating in the management of the enterprise.

A further trap for the unwary exists when the investment involves more than £500,000 and the market shares of the buyer and seller exceed 33 percent. The proposed investment must then be reviewed by the Department of Trade and Industry and referred to the Monopolies Commission for approval. The place of residence of the parties or on the place where such capital is invested.

Article 69 empowers the European Council, on a proposal from the European Commission, to issue the necessary directives for the progressive implementation of the provisions of Article 67. See STEUER, supra note 31, at ¶ 9.10, 9.11.

An exception exists where the new firm’s activities are centered in a development area or other areas which the Ministry of Trade and Industry designates.

52 STEUER, supra note 31, at ¶ 9.6 lists the criteria used as of April, 1972.

53 Foreign Investment in Britain, [1976] 1 DOING BUSINESS IN EUROPE (CCH) ¶ 23,653. An exception exists where the new firm’s activities are centered in a development area or other areas which the Ministry of Trade and Industry designates.

54 Id.

55 Id. Same exception applies to this criterion as applied to the first criterion. Further, this requirement is not necessary for financing needed for working capital purposes.

56 The Bank of England, supra note 42, at 24, explains when the general permission for the purchase of sterling securities is applicable. A purchase which gives the purchaser a 10% control of the equity is no longer considered to be a sterling securities purchase only. Therefore, specific permission must be obtained from the Bank of England for the purchase.

57 Id. at 22.
Monopolies Commission will investigate the possibility that the investment will give monopoly status to the American investor in the particular industry involved in the investment. The Monopolies Commission will then file a report with the Minister of Trade and Industry stating its reasons for or against the proposed investment. The Minister has the authority to make the final decision concerning this investment proposal.  

A final exchange control concern arises when a company, which is controlled by outsiders, wishes to repatriate profits or remit dividends to the parent company located in another country. Before this can be done, a specific application must be tendered to the Bank of England in accordance with the Exchange Control Act. The Bank will normally authorize such payments provided they represent earned trading profits or investment income. Capital which the foreign investor has directly invested may be repatriated to the parent company at any time, provided that the original entry of the capital into the U.K. was properly approved. Any subsequent loans from parent companies to their U.K. subsidiaries also require exchange control approval.

Permission for the establishment of a direct investment may be subject to specific conditions, especially when the investment is to be made in industries designated as nationally important industries by the Department of Trade and Industry. The foreign investor may be required to give assurances about his future intentions. The foreign investor may have to guarantee, for example, “the retention of a majority of British directors on the company’s board, the fulfillment of existing contractual obligations, commitment to a progressive increase in exports, maintenance of existing research and development programs, or a promise that there will be no reduction in the labor force.”

There are no sanctions that the U.K. Government can enforce, however, if the investing company breaches any of these assurances, nor is there any systematic procedure available to review the foreign company’s performance with respect to them. The British Government relies solely on the good faith and social responsibility of the foreign company to fulfill its assurances. Normally, the company’s own self-interest dictates adherence to the assurances. A breach of this good faith requirement will deeply impair the foreign company’s credibility. Future requests by such a company for investment permission will be denied or shackled with stiff regulations.

Upon full compliance with all of the requirements stipulated in the Exchange Control Act the local subsidiary or branch is endowed with all of the rights and liabilities accruing to a British company. The importance of this will be seen in the discussion dealing with the right of establishment under the E.E.C. Treaty.

4. Investment Incentives

In addition to exchange control requirements, the American investor must

58 King, supra note 27, at 34.
60 Id.
61 Foreign Investment in Britain, [1976] 1 Doing Business in Europe (CCH) ¶ 23,661.
also examine the various business incentives offered by the host country to attract and encourage direct investment to a particular industry or a particular geographic area experiencing a lack of economic growth, modernization, or productivity. Having experienced a decline of its older industries such as coal mining, engineering, and shipbuilding, the U.K. has incurred a high level of unemployment, minimal economic growth, an increase in old and obsolete plant and equipment, and net outward migration in the geographic areas where these industries once flourished. There is a present and urgent need for redevelopment of these areas.

Business incentives in the U.K. take the form of development grants or selective assistance. Development grants are awarded for the introduction of new plants, machinery, buildings, investment, and employee training in an assisted area. The schedule of development areas was expanded in 1972 to include over 65% of Great Britain. Grants for new plants and machinery were also expanded due to the government's recognition of the need for updating the depreciated and obsolete plant and equipment which presently exist in the U.K.

Selective assistance is provided in various forms, such as medium-term loans on preferential terms or removal grants of up to 80% of all reasonable costs necessary for the transfer of plant and machinery from one area of the U.K. into an assisted area. Finally, tax allowances on a national level is another form of business incentive employed by the U.K.

Any American company can take advantage of these incentives by informing the Department of Trade and Industry of its intention to invest in an assisted area of the U.K.

From this discussion it is apparent that, even though general concern about foreign direct investment and the demand for closer government supervision...
is on the increase, the United Kingdom has continued to maintain a favorable policy toward foreign direct investment, especially that direct investment originating in the U.S.A. This is so because the benefits which accrue to both the American multinational corporations and the U.K. economy are satisfactory to both parties.

The main concern for the American multinational corporation is the future of the U.K. economy. The rate of inflation, domestic demand and productivity are the main concerns. The apparent bleakness of the U.K. economy, however, may be offset by the fact that Great Britain's membership in the E.E.C. has opened a market of 200 million more customers to the U.K. based subsidiaries. Further offsetting the apparent cloud on the U.K. economy has been the prospect of the North Sea oil.

C. American Direct Investment in France

1. Direct Investment Defined

According to the French government a direct investment is: "(1) the purchase, creation or extension of a business, branch, or any partnership or sole proprietorship; (2) all other operations, which alone or simultaneously or successively with others, that enable a person or persons to obtain or increase control of a company . . . , whatever may be its form, or to insure the extension of a company already under its or their control."

The emphasis in this definition is on control. Government practice, in determining the extent of control involved in an inward direct investment, has been to look not only at the actual percentage of the domestic company's equity controlled by the investor, but also at other factors (including loans, patents, and licenses) which might contribute to the influence that the investor can use to gain control over the French enterprise. Consequently, even a small capital investment may constitute a direct investment when connected with one or more of these other factors. The difficulty, therefore, for a foreign investor is to determine whether his planned investment will be categorized as a direct investment subject to regulation by the Ministry of Finance.

Under part two of the above definition, a direct investment is one that involves an acquisition of more than 20% of the capital of a French company which is listed on the stock exchange. Moreover, direct investment includes direct or indirect loans or advances to a foreign-controlled company by its nonresident owners or by foreign enterprises in the same affiliated group, and direct or indirect guarantees furnished by nonresidents for their firms in France.

70 Foreign Investment in France, [1976] 1 DOING BUSINESS IN EUROPE (CCH) ¶ 22,654.
71 The Ministry of Finance requires that, before an inward direct investment may be made, a prior declaration or request for prior authorization be made by the foreign investor. "Specifically, a prior declaration or request for prior authorization must be made for an investment which involves the transfer of a participation in the capital of a French company between individuals or legal entities whose customary residence or head office is in a foreign country."
72 Foreign Investment in France, [1976] 1 DOING BUSINESS IN EUROPE (CCH) ¶ 30,753.
All transactions concerning the same company must be viewed together, even if each occurs at a separate time, in determining whether the transactions are to be treated as a single foreign direct investment. The French government utilizes an integration doctrine. Thus, if a French company is placed in a state of economic dependency because of the investment, whether an acquisition or otherwise, the company is considered as being under foreign control. The transactions, therefore, constitute a direct investment.

Prior to 1974, the only exemption from the requirement of a prior declaration and request for prior authorization for foreign investments involved an investment participation in 20% or less of the French company’s capital. At present, the exemption applies in cases of certain direct investment provided that the total amount of all direct investments made in any one French company within a one-year period does not exceed F.2 million. There are four categories of direct investment which fall within this exemption:

1. Increases in the capital of a French company in which foreign participation has previously been authorized, provided they do not result in any increase in the percentage participation of any non-resident shareholder in such company;
2. Increases in the capital allowances of, or funds available to, a French branch or establishment of a non-resident enterprise whose creation has been previously authorized;
3. Loans to a French company under foreign control made by its non-resident shareholders or by foreign enterprises of the same group, and loans made to a French establishment of a foreign company made either by such foreign company or foreign enterprises of the same group, provided that in each case the terms of the loan meet certain specified requirements;
4. Guarantees for the benefit of a French company accorded to it by non-residents who control it or by foreign enterprises of the same group relating to loans in foreign currency contracted by such company.

In every instance, the payments coming from non-residents to the French company must be the result of the sale of foreign currency on the foreign exchange market or French francs from external French franc accounts.

These exemptions rarely occur due to the fact that the French government exercises an unfettered discretion as to which transactions will qualify for the exemption. This is so regardless of whether the transaction would technically fit into one of the four categories described above. Consequently, almost all investment proposals will be subjected to the formal procedures outlined below.

2. Procedures Followed by French Government

Obtaining a prior authorization is very cumbersome. The French govern-

\[73\text{ See note 77 infra.}\]
\[74\text{ Decree No. 74-721 of Jul. 26, 1974.}\]
\[75\text{ Foreign Investment in France, [1976] 1 DOING BUSINESS IN EUROPE (GCH) ¶ 22,655.}\]
\[76\text{ Id. Decree No. 67-78 of Jan. 27, 1967, also made an exemption for those direct investments which originate in countries within the French franc zone, i.e., those countries whose central bank has an account agreement with the French Treasury. Further, the exemption extends to the increase of capital through the plowing back of the company’s undistributed earnings. See Arrêté of July 26, 1974, art. 1.}\]
ment has instituted a set of procedures which it follows in investigating a proposed direct investment to determine whether or not to grant a prior authorization. The investing company must file a prior declaration and request for prior authorization with the Ministry of Finance. This prior declaration and request for prior authorization must include: information about the potential investor; the company in which it plans to invest; the type and the amount of the investment; the means for financing the investment; and, the benefits it will contribute to the French economic welfare. The Ministry of Finance may consult any other governmental departments for comments and recommendations concerning the proposed investment prior to giving authorization for the investment. The Ministry of Finance must reply within sixty days to the non-resident investor. Failure to reply within this period acts as an approval of the proposed investment and the investor is free to proceed with the investment.

There is, however, a delay tactic available to the Ministry of Finance. The Ministry may, at any time within this sixty-day period, call for a postponement of the investment to allow for further investigation or to permit the investor to make changes to correct government objections. By resorting to this delaying tactic, the French government can obviously prevent a direct investment from taking place without providing any explanation to the investor. The net result is that the Ministry of Finance may grant or refuse requests for prior authorization without being required to state the grounds for its decision within any particular time period. This makes planning a direct investment in France extremely difficult, especially when a specific timetable is involved. Delay tactics may be used by the French government to discourage the direct investment. Moreover, the non-resident investor has no legal remedy available to him; these preventive practices are specifically contemplated by the French regulations.

Once the foreign investor has made a direct investment he must submit a report to the Ministry of Finance on special forms obtained from the Ministry within twenty days. This applies to all direct investments regardless of whether or not it was subject to a prior declaration. If no prior declaration was required for the direct investment at issue, then the report must be supplemented by a memorandum detailing the specifics of the direct investment.

3. Exchange Controls Used to Supplement Regulation of Direct Investment

Foreign direct investment is also regulated by exchange control require-

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77 The prior declaration or request for prior authorization is a declaration of intention made by the non-resident investor. It should include the specifics of the proposed investment and an estimate of the benefits the investment will bring to the French economy.

78 The benefits which the French government views favorably include a positive contribution to the balance of trade by increasing exports and decreasing imports, the introduction of new technology, an increase in employment and training of French workers, and development of the depressed areas of France. If the investment provides a net benefit to the French economy, the French government will be more inclined toward giving the needed authorization for the investment.

79 Torom & Craig, Developments in the Control of Foreign Investments in France, 70 Mich. L. Rev. 286 (1971).

80 Id.

81 See Arrêté of July 26, 1974, art. 3 and Circular of July 26, 1974.
ments. All transfers of capital between France and foreign countries or, within France, between residents and non-residents must be accomplished via an approved intermediary, unless the exchange operations have been granted a prior authorization by the Ministry of Finance. It is important to note that foreign individuals or entities become residents (for exchange control purposes only) once they have been established in France for a minimum of two years.

Two major types of transactions are prohibited unless prior authorization has been granted by the Ministry of Finance.

First, all transfer or exchange operations in France which lead to the establishment by a resident of foreign deposits or to the holding in France by a resident of means of payment against a foreign country. Second, the importation and exportation of (i) means of payment (drafts, checks, and notes) other than through an approved intermediary or, within specified limits, by resident or non-resident travelers or (in the case of the export of drafts) by importers and exporters, and (ii) securities other than through an approved intermediary.

A major consideration of the French Government when it decided to reimpose exchange controls in 1968 was the directive from the E.E.C. Commission ordering France to free from control those direct investments originating in other member states. France did not want to relinquish control over any direct investment, regardless of its place of origin. France believed its main obligation was to protect and promote the economic welfare of its people. It complied, however, with the European Commission's order. To compensate for the removal of regulation over direct investments originating in the E.E.C., France made parallel changes in its exchange control laws. These changes effectively subjected the investments coming from within the E.E.C. to all the regulations which existed prior to the European Commission's order.

Thus, under the present direct investment regulations, investments originating in other member states are subject only to the requirement of making a prior declaration with the Ministry of Finance. The E.E.C. investor is not required to make a request for prior authorization from the Ministry of Finance. The exchange controls, however, are applicable and require the E.E.C. investor to obtain authorization from the Ministry of Finance. This procedure, technically, does not conflict with the directive issued by the Commission. Consequently, France still maintains strict control over all foreign direct investment regardless of its place of origin.

82 Decree No. 68-1021 of Nov. 24, 1968, reimposed exchange controls as an answer to the growing financial crisis in France in 1968 because the French government feared that devaluation of the French franc might become necessary. For a further discussion concerning the reimposition of exchange controls, see Torem & Craig, supra note 79, at 289.

83 An approved intermediary includes a commercial bank approved by the Ministry of Finance. These banks handle the transactions which are permitted under a "general authorization" as set forth in Decree No. 68-1021, supra note 82.

84 Foreign Investment in France, [1976] 1 DOING BUSINESS IN EUROPE (CCH) ¶ 22,682.

85 Id. at ¶ 22,683.

86 Article 48 of the Treaty of Rome requires that all restrictions on the movement of workers within the Community must be abolished. Article 59 provides the same requirement with respect to freedom to provide services anywhere within the Community. Article 58 provides for the Freedom of Establishment within the Community. France's imposition of direct investment regulations on those investments originating within the E.E.C. was in direct violation of these articles.
Repatriation of capital must also be carried out through an approved intermediary bank. If remittance is for a sum less than F.1,000,000, it will usually be permitted without the investor having to obtain prior approval from the Ministry of Finance. In contrast, if the sum to be repatriated is greater than F.1,000,000 prior approval must be obtained from the Ministry of Finance. Prior approval is, however, generally granted.

4. France: The Most Restrictive Member State

French direct investment regulations are the most complex and severe of any Common Market country. There are two principal reasons for this attitude on the part of the French Government. One is that the French Government is concerned about the ability of the foreign-controlled subsidiary to exert a strong influence over those sectors of the domestic economy in which the investment is involved. The foreign parent company will often make financial and economic decisions for the French subsidiary. France believes that these decisions, which affect the French economy, are not being made with the French economic welfare in mind.

A prime example of this occurred in the late 1960's, when several American-owned subsidiaries closed down their French operations. This resulted in the laying-off of French laborers without consultation with the French Government. Consequently, the French Government was unable to provide for the immediate absorption of the workers into other areas of employment.

The second reason for France's restrictive attitude stems from its concern that American companies, by concentrating their investments in high technology areas, will take total control of these industries. The French Government does not want key sectors of its industry dominated by corporations which are under foreign control. Consequently, France's policy has been one of close scrutiny and tight control.

Generally, the French Government will grant permission for the establishment of a direct investment project, provided that the investment is not centered in an industry deemed to be critical by the French Government, or in an industry which is presently dominated by foreign-controlled companies. Should the investment project involve a critical industry or an industry which is heavily dominated by foreign-controlled companies, the investment will encounter severe resistance or complete refusal.

The best-known example of an investment refusal concerning a critical industry is that of General Electric's (G.E.) bid in 1964 to take a minority share in Compagnie des Machines Bull (Bull), the largest French computer company. (The computer industry is deemed to be a critical industry by the French Government.) In 1962, Bull found that it could not keep abreast of the technological advances of International Business Machines' (IBM) French

87 King, supra note 27, at 44.
88 KRAUSE, supra note 6, at 145.
89 Id.
subsidiary. It simply did not have the financial resources to maintain the research and development to compete with IBM. Bull reached a tentative agreement with G.E. to sell 700,000 new shares of stock to G.E. at $40 per share. This would give Bull an injection of $28 million and provide Bull with needed technical assistance and research facilities.

The Ministry of Finance refused to give the requisite prior authorization for the 20% acquisition by G.E. It felt that such an acquisition would result in the domination of Bull by G.E., and the domination of the French computer industry by American companies. The French Government preferred a French solution to Bull's problems. Two French electronics companies, C.S.F. and C.G.E., and an association of French banks headed by the Banque de Paris, would provide technical and financial assistance to Bull.

Subsequently, however, the French Government became convinced that only G.E. could provide the necessary technical and managerial assistance. As a result of this conviction, the French Government approved the formation of two companies, the manufacturing company controlled by Bull and the sales company controlled by G.E. A third company was formed by the French Government to do the marketing research and advertising. This third company was also to be controlled by Bull. Finally, the French Government required that Bull, alone, was to perform all of the French defense work in the computer field.

The French Government was thus extremely hostile to the original G.E. proposal in 1962 and severely limited G.E.'s functions in the final solution, achieved more than two years later. This incident illustrates how an American company can be delayed when attempting to make a direct investment in France. If an American company is confined by a rigid deadline for the direct investment, the potential of a long delay should be kept in mind when planning the timetable for the proposed direct investment. This is especially true when the proposed investment involves a critical sector of the French economy.

5. The Effect of the E.E.C. Treaty on French Policy

France has been compelled to relax some of its prohibitions due to the E.E.C. Treaty, which provides that the movement of products between member states must be free from tariffs. If the French Government prohibits a particular direct investment proposal, the American company may be able to establish that same investment in one of the other E.E.C. member states. As a result of the tariff-free movement of goods among member states, the U. S. subsidiary in another E.E.C. country will be able to market its products in France at prices competitive with domestically produced goods, despite the French Government's effort to prohibit the investment. Moreover, by compelling the U. S. company to invest elsewhere in the E.E.C., France will lose all benefits of the investment and thereby give a competitive advantage to the host country receiving the American company's direct investment. The lack of a common policy toward direct investment coming from outside of the E.E.C. thus enables U. S.

91 See Treaty of Rome, art. 9.
multinational corporations to gain obviously advantageous positions. Because of the disparity in policies, France has been forced to permit the establishment of foreign direct investments it normally would have refused.

6. Factors Helpful to Those Desiring to Invest in France

To help ensure approval of a proposed direct investment by the French Government the American company should consider emphasizing one or more of the following effects when it makes its proposal to the French Government. American companies which have included some of these factors have been looked upon favorably by the French Government. First, the American company should clearly point out that its investment will make a positive contribution to the French balance of trade. A positive contribution will result when the foreign investor manufactures products which France formerly had to import or when the foreign investor produces a product which France can export.

Second, any positive contribution to France's balance of payments should also be indicated. This will occur when the non-resident investor brings in foreign capital which must be converted into French francs on the official exchange market. Such a positive effect will not result if the financing is not done through franc financing on the French market. If an American company desires approval from the Ministry of Finance it must finance the investment with foreign currency or with French francs acquired from non-French money markets.

The U. S. company should also consider whether it needs to make the direct investment by acquiring an existing French enterprise or whether it can build a new plant. The French Government gives a more favorable treatment to an investment proposal which provides for the establishment of a new company rather than the acquisition of an existing French company, because the French Government prefers the influx of new plant, machinery, and equipment.

Another factor which will enhance an American company's chance of receiving the necessary authorization for its investment proposal is to guarantee to the French Government that it will establish a research facility in France. This is particularly critical if the industry involved in the direct investment concerns new scientific developments. France wants to be certain that its domestic technology will not be deprived of the new research developments. The French Government believes that French industry should participate in the new technological developments, not just be a recipient of new technology developed elsewhere.

Several regions in France are economically depressed. Investment applications offering to establish new plants in the listed development areas will receive a more enthusiastic response from the Ministry of Finance.

A final factor for the investing company to consider is that the French Government is afraid that direct investment will result in part of its economy

93 See Torem & Craig, supra note 79.
94 Id. at 318.
95 Id. at 320.
being controlled from outside of France. One way to help the French Government overcome this fear is to install French citizens in key positions in the parent company itself. IBM, for example, named a French native as the President of IBM World Trade Corporation. Several other members of the board of directors are also citizens of countries other than the U.S.A.

D. Conclusion

France’s attitude is still one of protectionism, due to its strong sense of nationalism. The U.K., on the other hand, maintains a broader worldwide outlook. This explains, in part, the divergence in policies concerning foreign direct investment. France is learning through experience that merely prohibiting undesired foreign investment is not the answer. French policy, generally, is to require authorization from the Ministry of Finance for all direct investment including that originating in other E.E.C. member states. The French Government maintains strict control over the amount and the nature of the foreign direct investment. Approval, however, will generally be given by the French Government unless a critical sector of the domestic economy is involved in the investment. The U.K. Government, in contrast, does not attempt to maintain close control over foreign direct investments. It employs a policy receptive to foreign direct investment, particularly that originating in the United States.

IV. Lack of a Common Commercial Policy Benefits U. S. Multinational Corporations

The divergence of the national laws of the member states and the lack of a common commercial policy have provided a vehicle whereby U. S. companies are able to gain an advantage over their European competitors. U. S. multinational corporations are economically strong enough to establish subsidiary operations throughout the Common Market. Most European companies lack such economic strength and are unable to increase that strength via transnational mergers with other European companies. Competition, therefore, for the U. S. subsidiary is primarily only on a national level.

Because of their diverse locations in the E.E.C., the U. S. multinational corporations can easily transfer goods, management personnel, technology, and capital from a subsidiary in one member state to one in another member state. A foreign multinational company, therefore, can draw on a vastly larger pool of resources than can its local national competitors.

This economic strength of U. S. multinational corporations, combined with the divergent national commercial policies with respect to treatment of foreign direct investment, has given the U. S. company another large advantage. The U. S. company is able to use its economic leverage in conjunction with a threat to establish its direct investment proposal elsewhere within the E.E.C. to gain favorable treatment from an otherwise reluctant host country. Consequently, when a member state imposes strict regulations on a U. S. direct investment

\[96\] Id. at 322.
proposal, the U. S. company, because of its economic strength, may be able to persuade that host country to relax its restrictions lest the U. S. company take its direct investment proposal to a member state which has a more favorable attitude.

It is important for a U. S. company seeking to establish a direct investment in an E.E.C. member state to understand that the restrictions imposed by a member state may be relaxed if the U. S. company is able to implement its economic leverage on the member state. The procedure involves negotiations between the member state government and the U. S. company, in which the U. S. company makes apparent the benefits that its direct investment will bring to the host country as well as its ability to gain favorable treatment elsewhere in the E.E.C. should the host country refuse to cooperate with the U. S. multinational corporation. Also, the U. S. company will be able to point out that if it goes elsewhere in the Common Market it can sell its goods tariff-free in the stubborn member state.

Because of the lack of a common commercial policy American multinational corporations can circumvent unfavorable treatment which they would otherwise be subjected to by a host government such as France. If France, for example, prohibited an American company from undertaking a direct investment project within its borders the company could seek permission to establish its direct investment in one of the other member states. If establishment is permitted by one of the other member states several consequences would follow. Despite the French refusal, the U. S. company could gain the right to establish itself in France by invoking the applicable establishment provisions of the Treaty of Rome. Further, France would forfeit to the other member state, which gave permission to the American company, the technology which this company possesses, the tax revenues this company will pay, and the employment and training of local laborers which this company will provide. Knowing these consequences, France may feel compelled to grant permission for the establishment of a foreign subsidiary even though such establishment would be contrary to France's national economic policies.

As a result of these pressures, the American multinational corporation is in a very favorable position. If it wishes to establish itself in a member state which either refuses to give permission or does give permission but imposes harsh regulations, it can threaten to establish itself elsewhere. The multinational corporation thereby forces the member state to choose between granting permission for the direct investment, contrary to its national economic policy, or permitting one of the other member states to reap the various incidental benefits associated with foreign direct investment.

V. Right of Establishment and Foreign Investors
Under the E.E.C. Treaty
A. Introduction

The legal and administrative treatment of foreign enterprises in E.E.C.

98 KRAUSE, supra note 6, at 146.
countries is characterized by the initial establishment and exchange control regulations imposed by the individual member states. The establishment and exchange control regulations of the United Kingdom and France have been discussed above. Once the foreign company has been granted permission to establish itself by one of the member states, it must do so in conformity with the company law of that member state. Upon completion of its establishment the new enterprise becomes entitled to treatment as a national of that member state under Article 58 of the E.E.C. Treaty. Community law affords several advantages in addition to those provided by the laws and economies of the individual member states and by the expanding market of the E.E.C. Community law can confer on foreign-owned enterprises the same rights and privileges enjoyed by locally owned enterprises in the Common Market; namely, Community treatment. This means that the company may set up anywhere within the E.E.C.

The E.E.C. Treaty states the conditions which must be fulfilled before a foreign enterprise may claim to be entitled to Community treatment. In regard to the right to establish agencies, branches, or subsidiaries in other member states Articles 52-58 of the Treaty are controlling. The provisions of the Treaty concerning the freedom of establishment, the freedom to move capital, goods, services, and workers across national boundaries are part of the Community Law under the jurisdiction of the European Court of Justice.

The European Court of Justice has jurisdiction only over those rights of foreign investors which arise under Community Law. The Court of Justice ensures uniform observance of the E.E.C. Treaty and of the rights of foreign investors under provisions of the Treaty. If a member state violates the protected rights of a foreign investor, however, the aggrieved individuals or corporations cannot file a complaint against a member state with the European Court. Article 169 permits the Commission to represent the interests of injured natural or legal persons before the Court of Justice. Further, a member state which believes that another member state has failed to fulfill its obligations under the Treaty may also bring the matter before the Court of Justice as provided in Article 170 of the E.E.C. Treaty. Consequently, only the Commission and a member state can bring a complaint against another member state for a violation of the rights guaranteed by the Treaty. A member state, therefore, which has violated the right of establishment under Articles 52-58 of an American Company which has qualified for treatment as a national of a member state cannot be so charged by the American company before the European Court of Justice.

The proper procedure for the American company is to bring this violation to the attention of the Commission or to that member state in which the company is already established. The Commission or that other member state may then bring the matter before the European Court of Justice. If, however, both of these bodies sympathize with the member state which is in technical violation of the Treaty, the American company will have no legal remedy available to

99 W. Balekjian, Legal Aspects of Foreign Investments in the European Economic Community 161 (1967).

100 The Treaty of Rome, art. 164, states that "the Court of Justice shall ensure that in the interpretation and application of this Treaty the law is observed."
it other than to pursue the matter in the courts of the member state that is violating the Treaty.

B. The Right of Establishment

The initial entry of a foreign direct investment in a member state, the form of direct investment selected, and the transfer and repatriation of capital are governed by the regulations and laws of each member state. Community law is irrelevant for these aspects of foreign direct investment, and will remain irrelevant until the nine member states can agree on a common commercial policy.

Once a foreign investor becomes “established” in one of the member states, Community law does become relevant for that investor if he desires to establish operations elsewhere within the Community. The right of establishment, in the context of Community law, has been defined as: “the right of nationals and of commercial or industrial legal entities assimilated to them, to move without legal restrictions set up for economic reasons, from the territory of one member state to that of another, for setting up or continuing a permanent commercial activity.”

The critical Treaty provision for a foreign enterprise wishing to satisfy the nationality principle and claim the right of establishment is Article 58. This article requires that companies or firms “formed in accordance with the laws of a member state and having their registered office (statutory seat), central administration (center of management), or principal place of business within the Community” be treated as natural persons who are nationals of that member state. This is important because Article 58 is written in terms of “natural persons.” The Treaty does not specify any requirements as to the nationality or residence of the owners or directors of a company seeking the right of establishment. Consequently, an American-owned subsidiary formed in accordance with the requirements stipulated in Article 58 will be treated as a national of the member state under whose laws it has been formed and will, therefore, qualify for the right of establishment under Article 52.

Freedom of establishment, however, is not completely unrestricted. It merely mandates that the host country treat nationals of other member states, with regard to the right of establishment, the same as it would treat its own citizens. Article 52 of the E.E.C. Treaty requires that restrictions on the freedom of establishment are to be abolished. The restrictions include “those on the setting up of agencies, branches, or subsidiaries by nationals of any member state established in the territory of any member state.” Article 52 refers specifically to nationals of any member state. Consequently, nationals of non-member states, even those who are located in a member state, will not qualify under Article 52.

This requirement that only nationals of member states will be given the

101 BALEKJIAN, supra note 99, at 200.
102 Id. at 205.
103 See Treaty of Rome, art. 52(1).
104 A foreign investor established in one E.E.C. nation and desiring to extend business operations into another E.E.C. nation must qualify under that host country’s national law. See BALEKJIAN, supra note 99, at 203 passim.
benefit of Article 52 is the first of two proscriptions set out in Article 52. A national of a non-member state who has a direct investment in one member state will not be able to bring himself within the requirements of Article 52 unless he has followed the establishment procedure outlined in Article 58 of the Treaty. By complying with the procedure the national of a non-member state will be accorded the status of a national of that member state in which it has made the investment for purposes of the E.E.C. Treaty. He must, however, be able to satisfy the second proscription contained in Article 52.

The second proscription in Article 52 is as follows. The phrase, "established in the territory of any member state" implies that there must be an "economic link" between the company claiming the right of establishment and the economy of the member state in which it is first established. If no such "economic link" can be proven, then persons, whether nationals or non-nationals of a member state, will not be entitled to claim the right of establishment under Article 52. Any foreign investor who desires to claim the right of establishment must satisfy both the nationality principle and the principle of an economic link with a member state.

The term "economic link" has posed some confusion in the member states. The economic link must be genuine. Some of the member states recognize a registered office as a genuine economic link, while several of the member states do not recognize a company as being formed in accordance with their laws unless it has a real office in the member state where the company is formed. The foreign investor must be careful to determine if the member state in which the investment is being made requires that a genuine office be established, not merely a registered office. Failure to comply with the municipal laws of the member state may prevent the new company from qualifying under Article 52.

Finally, a company which has been incorporated in a member state and has been established within the E.E.C. through a branch will qualify under Article 52 to establish its head office or branch operations in other member states only if it can bring itself within Article 58. If this same company, however, incorporates a subsidiary in the E.E.C., and if the subsidiary has its principal place of business or its center of management there, then the subsidiary, not the parent company, will qualify for the right of establishment under Article 52. This distinction between a branch and a subsidiary must be remembered by an American-owned company planning to make a direct investment in a member state if it is considering using Article 52 to establish operations in other member states.

Each member state still possesses full power and authority over foreign direct investment originating in countries outside the E.E.C. It is generally difficult, however, for a member state to prevent a foreign investor from escaping the discriminatory regulations imposed by that member state on foreign investors.

107 Lang, supra note 105, at 152.
108 Id. at 154.
109 Id.
If an American company is seeking establishment in France, for example, but the French regulations are unduly restrictive, the American company can gain access to France by bringing itself within the E.E.C. Treaty. The American company should follow the procedures outlined above, (i.e., fulfill the requirements in Articles 52-58 of the Treaty), by availing itself of the more liberal rules for non-resident establishment in one of the other member states. Once it has done so, it can gain access to France through its new European office via Article 52. France must, then, comply with the mandate of the Treaty and treat the proposed direct investment in the same manner as it would treat the same direct investment undertaken by any other national of a member state.

This unqualified right of establishment given by Article 52 is the general rule. There are, however, exceptions. If France, in the above example, can invoke one of these exceptions it will be able to deny the right of establishment to the American-owned subsidiary which has fully complied with Article 58. All that is necessary is that the French Government be able to prove the applicability of one of the recognized exceptions to the European Commission.

The European Council may, acting on a proposal from the Commission, rule that the Treaty provisions on the freedom of establishment should not apply to certain activities.110 Moreover, the law, regulation, or administrative action of a member state may limit the freedom of establishment, only if the member state convinces the Commission that such a limitation is essential to that member state's welfare, on grounds of public policy, public security, or public health.111 Additionally, there is a general provision which empowers the Commission to authorize a member state to take protective action if freedom of establishment would create serious difficulties "liable to persist in any sector of the economy or which could bring about serious deterioration in the economic situation of a given area."112

C. Conclusion

The Treaty enables a company established in one member state of the Community to establish itself in any other member state. This overrides any national policies or laws, with the few exceptions stated above, which discriminate against companies owned by nationals of non-member states.113 The Treaty, however, does not prevent companies owned by nationals of non-member states from being deprived of the right of establishment by a uniform law adopted by all member states.114 Indeed, France has been continually advocating the adoption of a common commercial policy to restrict foreign direct investment in European industry.115 The adoption of such a policy, however, is not to be expected in the near future. American companies, therefore, can use the E.E.C.

110 Treaty of Rome, art. 55.
111 Treaty of Rome, art. 56.
112 Treaty of Rome, art. 226.
113 LANG, supra note 105, at 150.
114 Id.
115 In 1963 France proposed to the Finance Ministers of the original six Member States at the Baden-Baden conference that the Commission prepare a study of U.S. investment in the E.E.C. for the purpose of laying the foundation for Community controls on U.S. investment. This proposal was not followed by the Commission as it was believed that the matter of U.S. investment should be handled on a national basis. See DICKIE, supra note 92, at 73.
Treaty to circumvent discriminatory prohibitions against the establishment of subsidiaries of American companies in a particular member state.

The benefit which Articles 52-58 can bestow on a company owned by nationals of non-member states is apparently unknown to many American companies. The companies which would probably benefit most from these provisions are those companies which do not possess sufficiently great economic or technological strength. These companies would be less successful in an attempt to induce the host government to grant permission for their direct investment on a non-discriminatory basis. Knowledge of the potential benefits which the right of establishment provisions of the E.E.C. Treaty can confer on such companies would be beneficial for any such company planning a direct investment in the European Common Market.

VI. Conclusion

The U. S. company seeking to make a direct investment within the E.E.C. must be aware of several factors which provide distinct advantages to the U. S. company. The member states of the Common Market control foreign direct investment on a national level due to the failure of the member states to formulate a common commercial policy. Each member state has instituted national commercial policies which it believes will best promote the economic welfare of its people. Consequently, the policies differ considerably. This divergence in national commercial policies provide a U. S. multinational corporation with the means through which it can gain an advantageous position within the Common Market should a member state refuse to grant permission for the investment or impose strict regulations on the investment. The U. S. multinational can use its economic power and the threat of establishing its direct investment elsewhere as leverage with which to gain favorable treatment from an otherwise reluctant member state.

Should the use of the U. S. multinational corporation's economic power and the threat of establishment elsewhere within the Common Market prove to be ineffective in persuading the member state to relax its restrictions, or should the U. S. company decide that it would be unwise to employ such a technique, there exists an alternative for the U. S. company to follow. If the company establishes its registered office, principal place of business, or its headquarters in a member state and fully complies with the requirements of Article 58 of the E.E.C. Treaty, it will be given the status of a national of that member state. Once the U. S. subsidiary has acquired this national status it must also comply with the second requirement contained in Article 52, namely: establish a genuine economic link with a member state. Upon complying with these two requirements the U. S. subsidiary may invoke Article 52 of the E.E.C. Treaty and claim the right to establish operations anywhere within the E.E.C.

Justin M. Stuhldreher

Many U.S. multinational Companies deal directly with the government of the country in which they plan to invest. They have never relied on the Right of Establishment provisions of the E.E.C. Treaty. Should a company encounter discriminatory treatment from a country or be denied permission to establish its investment, it could utilize the establishment provisions of the Treaty, provided that it qualifies under article 58.