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**The Role of Law, the Rule of Law
and the Rise
of Sovereign Wealth Funds:
The Need for a Greater External
and Internal Activism
of the European Union**

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THE ROLE OF LAW, THE RULE OF LAW AND THE RISE OF SOVEREIGN WEALTH FUNDS: THE NEED FOR A GREATER EXTERNAL AND INTERNAL *ACTIVISM* OF THE EUROPEAN UNION *

Daniele Gallo**

Abstract

From the point of view of international economic law and global governance studies, the principle of the *rule of law* should apply to all subjects who enter or aim to access the global market. Amongst them, a crucial role is nowadays played by the so-called 'sovereign investors', namely SWFs and SOEs.

This paper, which is based on the assumption that sovereign investment has become a major – albeit controversial – element in emerging patterns of governance in this century, deals more specifically with SWFs.

In order to put the rule of law 'in action' and take it 'seriously' with respect to SWFs, the paper focuses on the main concerns related to the rise of SWFs. In this respect, the main argument implied therein is that the quest for a fair balance between economic benefits deriving from the entry of SWFs in the EU market and the protection of national as well as European strategic/sensitive sectors must be pursued at the EU level and that, in doing so, the EU must be more *activist* and bolder.

The EU should give law a central role, regarding the market as an inherently political, institutional and social construct, rather than a self-referential *locus* that depends on its internal laws and dynamics. This seems even more urgent when market actors that, at least on paper, should be politically unbiased market-oriented investors, tend to act also as the long arm of State capitalism, that is, of foreign governments wishing to invest abroad in crucial socio-economic sectors and often connected with countries where the rule of law, in its multiple dimensions, is neither promoted nor respected.

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Summary: I. Conceptualizing the relationship between the rule of law and sovereign investment, with a focus on SWFs, international law and the EU's external action. 1. The multiple dimensions of the rule of law and the rise of sovereign investment: what are the main concepts, issues and concerns at stake with regard to sovereign wealth funds (SWFs)? 2. International *soft* law on SWFs and SWFs' self-regulation: the need for a greater role for international law as well as for the EU as a global actor in promoting transparency and accountability. – II. SWFs and the quest for a fair balance between market and non-market values within the EU. 1. The EU's institutional and jurisprudential minimalism *vis-à-vis* non-EU sovereign (direct) investments and the issue of the law applicable to SWFs: freedom of capital or freedom of establishment? 2. Member States and market restrictions: socio-

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economic protectionism, national security and the possible application of 'old' express derogations and/or 'new' mandatory requirements. – III. The need for greater internal and external activism on the part of the EU in relation to SWFs: the Union as a global promoter of the role of law and the rule of law, and the quest for a European golden share.

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- I. Conceptualizing the relationship between the rule of law and sovereign investment, with a focus on SWFs, international law and the EU's external action.
 1. The multiple dimensions of the rule of law and the rise of sovereign investment: what are the main concepts, issues and concerns at stake with regard to sovereign wealth funds (SWFs)?

As is well known, the rule of law, for which there is no single and exhaustive definition at national and international level, has different faces and intertwines with several concepts and categories.¹ The main idea implied in the rule of law is that any exercise of power should be subject to the law, no matter whether the subject vested with that power is a public or private actor/institution/entity.²

From the point of view of international economic law and global governance studies, this principle should apply to all subjects who enter or aim to access the global market. Amongst them, a crucial role is nowadays played by the so-called 'sovereign investors'.

By "sovereign investors" I mean public/private hybrids, namely sovereign wealth funds (SWFs)³ and state owned enterprises (SOEs)^{4,5} whose legal status and personality may vary significantly. Despite this diversity, they share two common features: they are all State-owned investment 'creatures' and they all invest both in strategic sectors which often (but not always) belong to the State, such as defence and national security, and in companies entrusted with the operation of public services that, although formally private, are under State influence.⁶ Therefore, they are public entities generally controlled by the government which, at least on paper⁷, behave as private operators/market investors at global level. In this sense they have been rightly defined, in the literature, as sovereign private entities, where the terms "sovereign" and "private" refer, respectively, to the legal status of SWFs and the supposed rationale behind their investments.⁸ SWFs reflect a recent trend: the assumption of an active

¹ On the theoretical premises and foundations implied in the elusive concept of the rule of law see the various papers presented at the Workshop. In the abundant literature, see, *ex multis*, Tamanaha (2004); Bingham (2010).

² See the Report of the UN Secretary-General of 16 March 2012, UN General Assembly, Sixty-sixth session, Agenda item 83, Delivering Justice: A programme of action to strengthen the rule of law at the national and international levels., p. 2, para I.2, where it is stated that the rule of law is "a principle of governance in which all persons, institutions and entities, public and private, including the state itself, are accountable to laws that are publicly promulgated, equally enforced and independently adjudicated, and which are consistent with international human rights norms and standards".

³ For an overview on SWFs, from a legal standpoint, see, *inter alia*, Catá Backer (2007-2008); Bassan (2011); Cuocolo, Miscia (2012).

⁴ For an overview on SOEs, see Catá Backer (2010: 59-74); Shapiro, Gliberman (2012).

⁵ For sovereign investors different than SWFs and SOEs see Barysch, Tilford, Whyte (2008: 2) and Bassanini (2011: XI).

⁶ On similarities and differences between SWFs and SOEs see Catá Backer (2010: 66-74); Bassan (2011: 21-23); Schmit Jongbloed, Sachs, Sauvart (2012).

⁷ I will return on the point below, in this and the following §§.

⁸ See Bassan (2011: 3-5).

role in the international market by sovereign/State capital – that is, by the State, which acts at once as a regulator, shareholder and private actor.

This paper, which is based on the assumption that sovereign investment has become a major – albeit controversial – element in emerging patterns of governance in this century, deals more specifically with SWFs rather than SOEs *et similia*, and it does so from the standpoint of international and EU law.⁹

The preliminary question to be asked is: what is a SWF?

A SWF is a fund or entity with a significant economic capacity that is instituted by the State and commonly established from balance of payments surpluses, official foreign currency operations, privatizations revenues, governmental transfer payments, fiscal surpluses, and above all from the receipts of commodities exports, in particular oil and gas.¹⁰ The legal framework of a SWF generally follows one of three approaches: according to the first, the SWF is established as a separate legal identity with full capacity to act and is governed by a specific constitutive law (e.g. the Kuwait Investment Authority); SWFs falling into the second category take the form of a state-owned corporation (e.g., Singapore's Temasek or China Investment Corporation); the third group of SWFs is constituted by a pool of assets without a separate legal identity which is owned by the state or its central bank (e.g. Alberta's Heritage Fund).¹¹

Countries establish SWFs for several purposes.¹² They are vested with different institutional tasks and their objectives may change over time.¹³ They manage domestic or third-country investments¹⁴ and aim at ensuring the intergenerational transfer of resources, the stabilization of public revenues and the funding of welfare spending.¹⁵ This definition of SWF and, therefore, the scope of this paper do not include other (new) forms of foreign State controlled investors, such as foreign currency reserve assets held by monetary authorities, government employee pension funds (funded by employees/employers contributions) and SOEs.¹⁶ As to the distinction between SOEs - such as GAZPROM, just to give a clear example - and SWFs, it must be stressed that, while the latter is a financial investor holding shares in companies providing different types of services, the former is an enterprise directly involved in manufacturing, operating infrastructure, extracting mineral or natural resources, and delivering services.¹⁷

In order to show the importance that a phenomenon such as sovereign investing has gradually acquired, capturing the attention of national and international policy makers

⁹ Catá Backer (2013: 2).

¹⁰ Sovereign wealth enterprises, that is, 'vehicles' owned and controlled by the State are different from SWFs.

¹¹ See also the Discussion of the GAPP, available at <http://www.iwg-swf.org/pubs/eng/santiagoprinciples.pdf>.

¹² See Barysch, Tilford, Whyte (2008: 2).

¹³ See Gordon, Niles (2012).

¹⁴ For what concerns the relationship between SWFs and the State who own them, as it has been previously noted, they are mostly under control of national authorities. However, some SWFs enjoy a larger degree of independence in their management. Moreover, as to the corporate governance structure of SWFs, there are several models which orient the funds' activities.

¹⁵ See Cuocolo, Miscia (2012: 8-9).

¹⁶ See the homepage of the Sovereign Wealth Institute, available at <http://www.swfinstitute.org/sovereign-wealth-fund/>.

¹⁷ See Ang (2010: 8-9).

worldwide, and to examine its impact on the content and extent of the rule of law, I will briefly provide some background facts on SWFs.¹⁸

Although SWFs have not grown at the rate that was anticipated before the economic and financial crisis exploded in 2008, they became more and more crucial financial players. The general prediction is that they will continue to grow in the future. At present, there are more than 100 SWFs active in the global arena, the majority of which belong to emerging countries,¹⁹ the Middle-East,²⁰ and Asia²¹. Therefore, the growth of SWFs is the symptom of a changeover in terms of wealth redistribution around the world: from Western industrial countries to countries which have become important players in international finance only over the last decades.

18 SWFs have estimated assets of more than \$50 billion, 9 have assets of more than \$100, 5 manage assets of more than \$500 billion, amongst which the Norwegian Government Pension Fund – Global (GPF) with about \$818 billion of assets, Abu Dhabi Investment Authority (\$773), Saudi Arabian SAMA Foreign Holdings (\$675), China Investment Corporation (\$572) and SAFE Investment Company (\$567).²² The non-homogeneous character of SWFs can be easily inferred by observing that amongst these top 5 SWFs there are many differences concerning a number of indices, e.g. in terms of compliance with transparency standards.²³ Not to mention the ties that said SWFs have with home countries which are poles apart in terms of respect of democracy and human rights.

As to the positive features characterizing SWFs as investors in the global economy, there is no doubt that they contribute to both global growth and financial stability by maintaining an open flow of resources for long-term investments, providing liquidity to Western companies and recapitalizing financial institutions hit by the crisis as happened with respect to many US banks during the 2008-2009 biennium.²⁴ In particular, during the economic and financial crisis they acted as stabilizers and indispensable lenders for numerous private institutions: the clear connection between them and the future of capital markets derives from this.²⁵

Having briefly outlined the main features of SWFs, the next step is to identify the main questions, issues and concerns raised by their proliferation at global level, using the rule of law as the main investigation tool.²⁶

As a first approximation, we may say that the main questions which arise are: what is the role of the law in the area of SWFs? What institutions are competent for the creation of the law governing those actors – at national, regional (European), and international level? Is the law governing SWFs mainly *hard* or *soft* law? What are the governance systems through

¹⁸ See above all the list of largest SWFs available at <http://www.swfinstitute.org/fund-rankings/>.

¹⁹ Such as National Welfare Fund and Reserve Fund, both Russian, and the Chilean Social and Economic Stabilization Fund.

²⁰ Such as Abu Dhabi Investment Authority, Saudi Arabian SAMA Foreign Holdings and Qatar Investment Authority.

²¹ Such as China Investment Corporation, SAFE Investment Company (China) and Government of Singapore Investment Corporation.

²² See also Bagnall, Truman (2013: 1-2) and Euler (2013: 1).

²³ See *infra*, in this § and in the following §§.

²⁴ On SWFs' investment in major global banks, many of which, like Merrill Lynch, were and still are in critical need of capital, see Butt, Shivdasani, Stendevad, Wyman (2008); Drezner (2008); Gelper (2009); Pistor (2009); Pistor (2012).

²⁵ On this aspect see Epstein, Rose (2009: 111).

²⁶ The (hot) issue of immunity, with regard to SWFs, is excluded from the scope of analysis of this paper; see Bassan (2011: 89-116).

which SWFs can or ought to govern themselves? These questions will be answered, with a focus on the EU's external action in the most relevant international *fora*, in the next §.

Another crucial question, from the point of view of EU law, will be answered in Sections II and III: is the law now in force (at international, European and national level) reaching the right balance between market and non-market interests?

In order to answer the above questions – which cut to the heart of the modern notion of global governance –, as well as to put the rule of law ‘in action’ and take it ‘seriously’ with respect to SWFs, I will focus on the main concerns and benefits related to the rise of SWFs. To do so, I will mention a number of interdependent concepts which, despite being autonomous principles or legal/conceptual categories, seem to act also as corollaries/sub-principles/constitutive elements of the rule of law: good governance, transparency/disclosure, accountability, human rights and democracy.²⁷ These terms are all strongly connected and particularly relevant when what is at stake are SWFs.²⁸

Investments by SWFs clearly raise delicate issues with regard to market behavior, political and economic motivations, and the protection of important national interests. As noted by Truman, one of the most renowned experts in the field, “[t]he reality is that government own SWFs, governments are political organizations, and it is naïve to pretend they are not”.²⁹ Or, as remarked by Lawrence Summers, President Obama’s former Chief economist, in a famous 2007 Financial Times op-ed, the concerns raised by SWFs are “profound” and touch on “the nature of global capitalism”.³⁰ The purchase of the Shin telecom businesses of then Thai Prime Minister Thaksin Shinawatra by Singapore’s SWK Tamesek is paradigmatic, in that it reveals the high degree of politicization of investment decisions made by SWFs.³¹ Another example is the purchase of \$300 million Costa Rican bonds by China, not only but also through the Chinese SWF SAFE, as a means to pressure Costa Rica to drop its diplomatic recognition of Taiwan. Moreover, even the threat of investment withdrawal could hide a political bias, partially calling into question the “negotiating tactics of target nations”.³²

The most widespread fear is that SWFs may act under the pressure of the home State with the aim of advancing and achieving political and geo-strategic goals, rather than purely acting as market investors that intend to pursue economic objectives. Therefore, SWFs’ investment decisions – especially when they take the form of mergers and acquisitions – may harm the socio-political-economic stability of the host State. More in particular, SWFs may endanger national security, lead to an appropriation of technological information by foreign States, influence the economic behavior of the host State’s companies providing essential public services, distort competition by favoring non-market principles and criteria, control national economic ‘champions’, industrial complexes and critical infrastructure, and acquire limited natural resources.³³ The issue is particularly problematic when the home State which owns

²⁷ In this regard see the Resolution adopted by the UN General Assembly 66/102 “The rule of law at the national and international levels” of 9 December 2011 and the Speech 13/677 of 4 September 2013 by V. Reading, Vice-President of the European Commission, on “The EU and the Rule of Law – What next?”.

²⁸ Plus, some of them can be a source of difficulty at operational level: for instance, it is easier to request SWFs to be transparent in their functioning, i.e. to provide public information on their legal basis, organization and financing decisions (not to obtain that they will do so ... which is quite a different issue!) than requiring their compliance with good governance principles.

²⁹ Truman (2010: 41).

³⁰ As reported by Gordon, Niles (2012: 32).

³¹ On this example see the considerations by Schmit Jongbloed, Sachs, Sauvart (2012: 11).

³² In these terms Gordon, Niles (2012: 32).

³³ See Rose (2008) and Cooke (2009).

aggressive SWFs does not exactly put democracy and human rights at the top of its hierarchy of values. The case of the investments of the Libyan Investment Authority in Finmeccanica, the greatest Italian defence company, as well as in Unicredit, one of the largest European financial institutions, clearly illustrates this point.

In short, the main criticism against SWFs lies, more broadly, in the mercantilist role³⁴ of an imperialist-capitalist State³⁵ that assists and stimulates the spread of its legal and economic ramifications in the global arena. The opponents of the entry of SWFs in national markets maintain that such actors want to acquire control of pivotal economic and sensitive sectors, taking advantage of the privatizations process that has taken place in almost all States and opened up key industrial sectors to not only to national, but also foreign market operators.

Another principal area of concern, for both the host and home states of SWFs, is the level of transparency of their structure, governance, amount for investment, goals, and investment strategies.³⁶ As a matter of fact, there is no doubt that the SWFs whose investments are aimed at attaining political objectives, rather than based on business-oriented purposes, are those that are more likely to be opaque.³⁷ It is true that also hedge funds and private equity firms are opaque, but the point is that they are driven by private goals: a more serious threat for host States as well as for market operators is that public entities which should pursue solely commercial goals are actually influenced by political attitudes.³⁸

The lack of transparency of many SWFs has serious consequences, since it does not allow for the building of trust (especially) between Western countries and SWFs³⁹, impedes a full understanding of their market efficiency and regulatory compliance, and makes it difficult to evaluate whether non-market purposes run the risk of making SWFs investment strategies inefficient. Furthermore, the fact that SWFs do not disclose these strategies gives rise to asymmetric information⁴⁰, which occurs “when one party has better information than the counterparty”⁴¹, i.e. when the recipient State is unable to ascertain the accuracy of that information or even to acquire information on the very SWFs that invest in its territory.

Furthermore, the need for transparency lies in the fact that the large amount of national wealth invested by SWFs abroad is owned by the Public of the home State.⁴² Indeed, before the emergence of SWFs a government’s earnings were usually likely to increase the national budget and the Central Bank’s foreign exchange reserves, ensuring safe revenue for its citizens.⁴³ Therefore, the transparency of SWFs remains a matter of public concern, not only in host countries but also in home countries.⁴⁴

³⁴ Of new *mercantilism* speak Gilson, Milhaupt (2008).

³⁵ See the reflections made by Schweitzer (2011: 79-81).

³⁶ On the individuation of five areas of SWF transparency (political, procedural, policy, operational, performance) see the analysis carried out by Dixon (2013).

³⁷ Schmit Jongbloed, Sachs, Sauvart (2012: 14).

³⁸ On a comparison between SWFs, hedge funds and private equity firms see Gordon, Niles (2012: 31).

³⁹ Saxon (2009: 709-710).

⁴⁰ See Rose (2008: 114), Wong (2009) and De Bellis (2011).

⁴¹ Wong (2009: 1082).

⁴² Bagnall, Truman (2013: 1).

⁴³ Sachs (2012: XXII).

⁴⁴ As stressed by Mehrpouya (2013: 1), “transparency demands in the transnational space rely on two different normative bases of ‘information needs of market actors’ and ‘democratic information rights of the public’”.

Closely connected with the issue of transparency is the question of accountability. When citizens can be informed about government policies and governments know that their citizens are watching them, their incentives to create good policies grow. In the Report prepared by the Commission on the Measurement of Economic Performance and Social Progress, composed of J.-P. Fitoussi, A. Sen and J. Stiglitz, accountability of government is defined as a strong instrument for good government performance.⁴⁵ Some scholars even maintain that transparency is important insofar as it is instrumental for ensuring the accountability of SWFs.

But what does 'accountability' mean in this area? It does not necessarily imply the power to impose formal sanctions⁴⁶. Rather, when accountability is referred to SWFs, what must be understood is to whom SWFs must be held accountable and whether there are consequences if their behavior is not in line with the prerogatives of the different stakeholders concerned.

The stakeholders involved are⁴⁷: the citizens of the SWF home country, who have an interest in how the government invests national collective assets abroad; the public authorities of the home State; the market participants that are active in the global financial arena; the public authorities and the citizens of the host country.

In the case of the first group of stakeholders, we may speak of internal accountability, which is expressed at the political level and whose consequences vary depending on whether the country concerned is democratic or non-democratic and according to the importance of certain concerns for the State. For example, the citizens of democratic countries, by holding their political leaders accountable for what they do, may disapprove, whether through their political representatives or through elections, the government's decision regarding SWFs. In those countries where the respect of fundamental rights at the international level is considered a highly sensitive issue, the political debate has led the government to impose an obligation on their SWFs to invest in compliance with ethical and environmental standards/rules: such is the case of the Norwegian GPF, which is bound to make responsible investments under the Ethics Guidelines⁴⁸ adopted by the Norwegian Ministry of Finance.⁴⁹ These Guidelines have now become part of an integrated system of responsible investing "that is meant to serve as a set of legal qualitative and policy standards governing the sorts of investments that the Fund can make". Indeed, they forbid investment in companies that engage in certain economic activities, such as companies that produce weapons that through normal use may violate fundamental humanitarian principles, or those that produce tobacco or sell weapons or other military goods.⁵⁰

As to the authorities of the SWF country, i.e. the second stakeholder involved, sanctions may be imposed by requesting and obtaining that the management of the fund resign when it is not satisfied with its investment policy. The managers of the SWF may be generally deemed accountable to the legislature, as in the case of both the GPF and the Kuwait Investment Authority, or to a Board, as in the case of the Australia Future Fund.⁵¹

⁴⁵ See <http://www.stiglitz-sen-fitoussi.fr/en/index.htm>.

⁴⁶ Bovens (2007: 257).

⁴⁷ See De Bellis (2011: 370).

⁴⁸ See Guidelines for the Observation and Exclusion of Companies from the Government Pension Fund Global's Investment Universe of 1 March 2010, available at http://www.regjeringen.no/en/sub/styrer-rad-utvalg/ethics_council/ethicalguidelines.html?id=425277.

⁴⁹ On this issue and others concerning GPF see Catá Backer (2013).

⁵⁰ As noted by Catá Backer (2013: 21-22).

⁵¹ See Ang (2010).

The third group of stakeholders corresponds to credit rating agencies which can assess the fund's investment policies, an assessment based on which other financial/market operators may take their decisions.⁵²

With regard to the last group, which includes the national authorities and citizens of the host country, accountability is closely connected with disclosure, since those authorities may take into account in their decisions both institutional and market governance patterns and, if necessary, impose a 'sanction' on the SWF by erecting a protectionist barrier against its entry in the national market of that country. What we have said with regard to the first group of stakeholders holds true also in this case, since SWFs that have ties to non-democratic countries where the rule of law is violated (e.g., in terms of human rights protection), or SWFs which are characterized by a serious lack of transparency, may not be very welcome.⁵³

All of the above should not lead one to assume that SWFs *naturally* and always tend to endanger the national security and even the political and economic independence of the receiving State. As a matter of fact, at present there are suspicions, but still no clear evidence of violations or political attitudes and purposes on the part of SWFs.⁵⁴ In this regard, many scholars are right when they observe that there are dangerously protectionist impulses behind the distrust in SWFs, impulses which are a serious threat to economic growth as well as international trade and finance.

However, even those observers who, disagreeing with the view that SWFs may pose serious risks for hosting States, point out the need to opt for an open investment environment consider the lack of transparency and accountability a primary problem.⁵⁵ This means that the criticism according to which SWFs' investments are politically motivated cannot be confused with the issue of transparency and accountability. We could also say that, if there are no data on violations committed by SWFs, it is not because these violations have never occurred, but only because they do not become apparent due to a lack of transparency. Indeed, the interconnected issues of transparency and accountability – which, moreover, are not based on suspicions, assumptions or possible risks, but on facts – lie at the hearth of the contemporary discussion on the regulation of SWFs. For this reason, the next §§ will be mainly devoted to these two issues.

2. International *soft* law on SWFs and SWFs' self-regulation: the need for a greater role for international law as well as for the EU as a global actor in promoting transparency and accountability.

The main international forum within which a regulatory framework on SWFs has been established is the International Monetary Fund (IMF), or, more precisely, the International Working Group of SWFs (IWG) set up by the IMF itself on 30 April-1 May 2008 and composed of 25 representatives from IMF member States owning a SWF. In October 2008 – that is, just 5 months after its establishment - the IWG adopted the Generally Accepted Principles and Practices⁵⁶ for Sovereign Wealth Funds (GAPP), also known as the Santiago Principles.⁵⁷ The

⁵² On this point see De Bellis (2011: 371).

⁵³ At national level see the analysis carried out, *inter alia*, by Schmit Jongbloed, Sachs, Sauvart (2012: 16-21), Clodfelter, Guerrero (2012), Jost (2012), Lowery (2012), Mendeshall (2012), Safarian (2012); on the erection of national barriers against SWFs see also *infra*, Section II.

⁵⁴ See Barysch, Tilford, Whyte (2008: 6-8).

⁵⁵ As noted by De Bellis (2011: 374).

⁵⁶ On the international soft law regulating sovereign investment, including the *Generally Accepted Principles and Practices for SFWs* – so-called 'Santiago principles' – available at <http://www.iwg->

GAPP constitute a voluntary set of 24 principles (divided into sub-principles) and practices that properly reflect appropriate governance arrangements as well as the conduct of investment practices by SWFs on a prudent and sound basis.⁵⁸

On 5-6 April 2009, the IWG developed into a permanent International Forum of SWFs (IFSWF). The IFSWF is not an international/supranational institution or a binding authority⁵⁹, but a network of SWFs endorsing the GAPP whose purpose is to share views on issues of common interest and on the application of the Santiago principles, including from an operational and technical standpoint. Thus, the IMF is the context within which the States have drawn up a soft law instrument. The inter-state level, however, has laid the basis for a shift from a government-controlled standard-setting process to a self-regulation on the part of SWFs, which, indeed, are the only members of the International Forum.

Concerning the role of the rule of law in relation to the GAPP, I believe that these principles must be warmly welcomed, with regard to both transparency and accountability, since they are designed to underwrite the legitimacy of SWFs, as well as to define them as institutional investors in global capital markets that, like other conventional beneficiary institutions, must act solely in the pursuit of risk-adjusted financial returns. Hence, the GAPP are indeed a significant example of transnational institution building and soft law development aimed at improving the transparency, accountability and, more generally, the good governance of SWFs under the supervision of an international organization.

I will focus on a number of the most important principles and sub-principles aimed at promoting the SWFs as sound and 'healthy' market operators, in the light of the explanation and commentaries provided by the IWG itself.⁶⁰

Subprinciple 1.2 states that the key features of the SWF's legal basis and structure, as well as the legal relationship between the SWF and other state bodies, should be publicly disclosed. Here, the aim is to enhance the public understanding of and confidence in the mandate to manage public monies as well as the comprehension of the responsibilities of the SWF in the context of its role within a constellation of government bodies and other public entities.

Principle 2 provides that the policy purpose of the SWF should be clearly defined and publicly disclosed. The rationale here is to stimulate appropriate investment strategies based on economic and financial objectives, while other types of purposes should be narrowly defined and explicitly mandated. Therefore, non-commercial purposes are not excluded *a priori*; the only express prohibition is that the SWFs cannot undertake investment with the intention to fulfill, whether directly or indirectly, geopolitical goals on behalf of the government. In addition, subprinciple 19.1 states that "if investment decisions are subject to other than economic and financial considerations, these should be clearly set out in the investment policy and be publicly disclosed". This seeks to prevent SWFs from hiding political or geo-strategic objectives behind the exclusion of certain investments on social, ethical, or religious grounds⁶¹ (e.g., Kuwait, New Zealand, and Norway), or for other reasons.

swf.org/pubs/eng/santiagoprinciples.pdf, as well as on the need for global standards for SWFs see Bassan (2011: 39-88); De Bellis (2011); Das, Mazarei, Stuart (2012); Gordon, Gaukrodger (2012).

⁵⁷ Available at <http://www.iwg-swf.org/pubs/gapplist.htm>.

⁵⁸ See the Introduction of the Report drafted by the IWG, available at <http://www.iwg-swf.org/pubs/eng/santiagoprinciples.pdf>.

⁵⁹ As clarified in the Kuwait Declaration through which the IFSWS has been established.

⁶⁰ Available at <http://www.iwg-swf.org/pubs/gapplist.htm>

⁶¹ As is the case of the Norwegian Government Pension Fund – Global as well as of the Kuwait Investment Authority; see the commentary on the sub-principle 19.1.

Principle 4 requires SWFs to disclose policies, rules, procedures and arrangements in relation to the SWF's funding and spending operations as well as to withdrawals from the SWF. In particular, the disclosure of the source of funding ensures a better understanding of the uses of public monies, with the result of fostering and promoting accountability. The same is required by the Principle 11, according to which an annual report and accompanying financial statements on the SWF's operations and performance – which must be audited annually as established by Principle 12 – should be prepared in a timely fashion and in accordance with recognized international or national accounting standards in a consistent manner. Principle 23, moreover, provides that the assets and investment performance of the SWF should be measured and reported to the owner according to clearly defined principles or standards.

According to the Principle 6, the governance framework for the SWF should be sound and establish a clear and effective division of roles and responsibilities in order to facilitate accountability and operational independence in the management of the SWF to pursue its objectives. At the core of the principle lies the intention of the IWG to ensure that investment decisions are based on economic and financial considerations and free of political influence and interference. Principle 6 is connected with principle 16, which focuses on the need for SWFs' managers to be operationally independent from their owner.

Closely connected with Principle 6 and Principle 16 is Principle 9, which provides that the management of the SWF should act in an independent manner, i.e., in the interest of the fund and not in order to attain political objectives. This means that the government should determine the broad policy purposes of the SWF, but it should not to intervene in decisions concerning specific investments.

As to the accountability framework for SWFs, Principle 10 states that it should be clearly defined in the relevant legislation, charter, other constitutive documents, or management agreement.

Principle 13 requires SWFs to adopt professional and ethical standards, which should be clearly defined and made known to the members of the SWF's governing body(ies), management, and staff. This is a crucial principle, since it aims at ensuring the soundness and integrity of a SWF's operations. To this end, it requires that members of the governing body(ies), managers, and staff should be appropriately qualified and well-trained and should be subject to minimum professional standards. Fundamental, in this regard, is the explanation that "to the extent applicable, the governing body(ies) should require establishment of a code of conduct for all members of the governing body(ies), management, and staff, including compliance programs".

Principle 15 focuses on SWF activities in recipient countries and, by doing so, points out that SWF operations should be conducted in compliance with all applicable regulatory and disclosure requirements of the countries in which they operate.

Principle 20 aims at promoting the fair competition of SWFs with private entities, providing that SWFs should not seek or take advantage of privileged information or inappropriate influence by the broader government in competing with private entities, for instance with regard to advantages arising from privileged access to market sensitive information.

Finally, Principle 24 is of crucial importance, since it ensures that all previous principles are actually put into practice: "a process of regular review of the implementation of the GAPP should be engaged in by or on behalf of the SWF". The implementation can be verified through self-assessment performed by the SWF along with its owner, or other mechanisms such as third-party verification as determined by the SWF or its owner or governing body(ies).

From all the above, it can be inferred that the Santiago principles are certainly a step in the right direction with regard to promoting transparency and accountability and, therefore, the

respect of the rule of law by SWFs and their home States. Hence, the real issue is not the type of regulation established by the GAPP but, rather, the fact that the extremely positive regulatory activism promoted by the States in the context of the IMF has provided no means to ensure the constant control over the implementation of those principles. Indeed, Principle 24 has remained a dead letter.

The idea to rely only on a voluntary approach through the adoption of codes of conduct on the part of SWFs, even though not the best *a priori* solution, is not to be disregarded *per se*. The problem here is that the GAPP, rather than being the first of a series of regulatory initiatives focused on a crucial aspect such as implementation, has not been followed by any significant action at the global level. In this sense, what happened in the field of corporate social responsibility (CSR) with regard to (private) multinational enterprises (MNEs) is paradigmatic: as is well known, in that case a number of significant initiatives at the international level (UN, OECD, etc.) have led the States to follow-up the drafting of the relevant guidelines with further action..

Besides the IMF⁶², there is another *forum* in which States have adopted soft law instruments to reconcile the need to preserve and expand an open international investment environment with their duty to protect the essential security interests of the population.⁶³ I am referring to the Investment Committee of the Organization for Economic Co-operation and Development (OECD), which on 8 October 2008 adopted the Guidance on recipient country policies towards SWFs, subsequently presented in Washington D.C. on 11 October 2008 to the International Monetary and Financial Committee of the IMF, as a contribution to the drafting of the GAPP. The Guidance⁶⁴ is divided in three parts: the OECD Declaration on SWFs and recipient country policies; the Guidance reaffirming the relevance of long standing OECD investment principles; and the Guidelines for recipient country investment policies relating to national security. The first document, prepared by the Finance Ministers who met at the OECD in June 2008, provides a high level political support for OECD Guidance with the aim to increase its status as a crucial source of international (investment) law. The second document is aimed at reaffirming the relevance of long standing OECD investment principles (first adopted in 1961) for recipient countries' policies concerning (also) SWFs, among which: non-discrimination in the treatment of foreign investors and similar domestic investors, stand-still (not to introduce new restrictive trade measures), progressive and unilateral liberalization, i.e. not to adopt measures based on reciprocity. Finally, the third document provides a series of recommendations establishing the right of investment-recipient States to take measures aimed at protecting essential security interests, in compliance with the principles of non-discrimination and regulatory proportionality. In this last part, which concerns mainly – but not only – SWFs (even though the term “SWF” is never mentioned in the text), the focus is on transparency/predictability and accountability, but from the angle of the measures adopted by the host States. In particular//More specifically, recipient countries should make decisions about blocking or limiting SWF investments at as an instrument of last resort and at a high political level. They should discuss these decisions publicly and ensure that the authorities responsible for restrictive investment policy measures are accountable to the citizens on whose behalf these measures are taken.

⁶² See also the work of the Global Reporting Initiative; see, more specifically, the 2013 Report on sustainability and transparency, which deals with the issue of SWFs, available at <https://www.globalreporting.org/resourcelibrary/Carrots-And-Sticks-Promoting-Transparency-And-Sustainability.pdf>.

⁶³ Instead, the hard law level has been jealously defended by national States; on the topic see *supra*, at footnote 53.

⁶⁴ Available at <http://www.oecd.org/daf/inv/investment-policy/oecdguidanceonsovereignwealthfunds.htm>.

As already noted with regard to the GAPP, the OECD Guidance must be warmly welcomed. However, two observations must be made in this respect, which confirm the current regulatory minimalism on SWFs and the rule of law at international level. First, even though the Guidance grants recipient States the power to adopt restrictive measures, it is important to stress that the requirements of transparency and accountability are mentioned only in relation to those measures rather than to SWFs. Second, a simple look at the OECD website – which contains information on the organization’s events, reports, declarations, speeches and approach to SWF – is enough to understand that no further steps have been taken towards making more specific the provisions of guidelines which still seem too vague and, above all, towards providing for an efficient system of compliance, or at least of supervision, despite suggestions in this sense were made in the OECD Guidance.

The EU has supported multilateral efforts under the auspices of both the IMF and the OECD. Its role has been important in the drafting of the guidelines and in drawing attention, in those *fora*, to good governance and transparency, as already clarified in its Communication of 27 February 2008, where it also stressed the need for an open dialogue with SWF owners and recognized the benefits of a global approach to a common framework for SWF investments.

What the EU should do, however, is to play a leading role at the global level with the aim of promoting in a more effective way the transparency and accountability of SWFs, trying to lay the basis for a sound regulation in the field and an adequate monitoring mechanism, or at least for the adoption of a transparency index in the framework of the IMF or OECD. This index would function as a method of rating transparency in respect to SWFs, based on the precedent of the Linaburg-Maduell Transparency Index, which, with its 10 essential principles, was developed at the Sovereign Wealth Fund Institute by Carl Linaburg and Michael Maduell⁶⁵.

As I will make clear below⁶⁶, there is, in short, a specific need with regard to SWFs and their respect of fundamental dimensions of the rule of law: the need for – if not a binding institution and binding international rules (a result which, at present, it would be unrealistic to expect) – a forum which may ensure a more effective and constant regulation of SWFs, by assigning monitoring and follow-up tasks to a specific entity vested with the power to make public the results of said monitoring, as well as to disclose a SWF’s refusal to be monitored.

The Santiago principles represent a very positive step towards a sound legal framework, aimed at underpinning a robust institutional and governance structure of the SWF and a clear delineation of responsibilities between the SWF and other governmental entities. However, compliance with the GAPP has remained measured and only few SWFs have sought to mitigate the concerns raised by the lack of transparency and accountability. Due to the choice to rely only on self-regulation in order to solve these issues, SWFs like the highly ‘*politically correct*’ Norwegian GPF – whose activities, regulated also by ethical guidelines, are characterized by a high degree of transparency as well as by the respect of human rights and environmental standards –⁶⁷, have been very rare.⁶⁸

II. SWFs and the quest for a fair balance between market and non-market values within the EU.

⁶⁵ Available at <http://www.swfinstitute.org/statistics-research/linaburg-maduell-transparency-index/>.

⁶⁶ See *infra*, Section III.

⁶⁷ See *supra*, § 1.

⁶⁸ On the topic see Gordon, Niles (2012: 42-56).

1. The EU's institutional and jurisprudential minimalism *vis-à-vis* non-EU sovereign (direct) investments and the issue of the law applicable to SWFs: freedom of capital or freedom of establishment?

In this part of the paper I will deal with SWFs that enter or aim to access the EU market.

The problem is twofold: whether the golden shares held by the State in EU companies which are the target of SWFs are admissible under EU law and whether the State can (more or less) expressly forbid the entry of said non-EU actors into the EU market.⁶⁹ The EU has provided no clear solution to this problem and to all concerns indicated above, § 1, Section I: there are no judgments on this issue nor binding EU instruments aimed at regulating SWFs in the European market or their investment limitations, apart from the limitations concerning non-EU operators provided for in sectorial legislation concerning electricity, gas and air transport.⁷⁰

In the aforementioned Communication of 27 February 2008, the Commission has made some important observations to address the risk that protectionist reflexes could damage the integrity of the single market. This means that at the center of the Commission's attention lies the problem of protectionism rather than the various issues which revolve around the content and extent of the rule of law, in its multiple dimensions highlighted above (transparency, accountability, democracy, human rights etc.). This does not mean that those issues are not covered in the Communication; however, they deserved to have been dealt with in more depth. The Commission clarified that "[t]he legitimate interests of citizens and market operators in Europe, as well as the benefits of certainty to the SWFs themselves, point to the need for increased transparency, predictability and coherence in this area".⁷¹ It is true that the Communication emphasizes that specific concerns relate to "the opaque way in which some SWFs function and their possible use as an instrument to gain strategic control" and that there is a case for "enhancing the transparency, predictability and accountability of SWF operations".⁷² The point, however, is that these concerns should be seen, according to the Commission, as inputs for a process of regulation to be carried out at global (IMF, OECD, etc.)⁷³ rather than at EU level.⁷⁴

After this very brief overview of the current situation of the EU legislation and jurisprudence on SWFs, a crucial question to be examined concerns the law applicable to State-held golden shares: freedom of establishment or free movement of capital?⁷⁵ Opting between the two sets of provisions is not so important with regard to intra-EU trade since, in relation to capital and establishment, the approach adopted in the case law on the scope of market restrictions and that taken in decisions concerning general interest justifications have been very similar.⁷⁶ Choosing between freedom of capital and freedom of establishment becomes essential, however, in connection with third country investment because, insofar as

⁶⁹ For a discussion of SWFs in a European perspective see Barysch, Tilford (2008); Schweitzer (2010); Chaisse (2012).

⁷⁰ See Art. 11 of Directive 2009/72/CE and Directive 2009/73/CE as well as Art. 4 of Regulation 2407/92. On the topic see Torrent (2012: 558-561).

⁷¹ See para. I of the Communication.

⁷² See paras II. 2.2 and III.3.2 of the Communication.

⁷³ On this issue see *supra*, § 2, Section I.

⁷⁴ See paras IV.4.3 and V of the Communication.

⁷⁵ On this issue, from the point of view of the concept of solidarity, see Gallo (2014).

⁷⁶ See O'Brien (2010: 257).

non-EU investors are concerned, the rules on capital, as is well known, have a wider scope of application *ratione personae* than those on establishment. As a consequence, SWFs may invoke Art. 63, but not Art. 49, when claiming before an EU national court that their rights have been infringed by a special power held by a government of an EU Member State in a privatised company operating within its territory.

In its first decisions on the matter⁷⁷, the Court focused its reasoning only on the rules relating to capital movements, in line with the so-called “centre-of-gravity” approach first adopted in *Fidium Finanz* (3 October 2006) with regard to the banking sector: in the event of an overlap between Art. 63 and Art. 49, the ECJ may apply “only that provision which it finds to be most directly affected if the other is thought to be ‘entirely secondary’”.⁷⁸ Subsequent case law⁷⁹, however, saw growing importance being attached to Articles 49 *et seq.* TFEU, in line with the so-called “Baars criterion”⁸⁰, according to which, when a national of a Member State has a holding in the capital of a company established in another Member State, the applicable national legislation falls within the purpose and scope of the freedom of establishment if that holding “gives him definite influence over the company’s decisions and allows him to determine its activities”.⁸¹ In later years, the Luxembourg court took an opposite view to that of *Commission v. Italy* of 26 March 2009, once again revising its previous jurisprudence. More precisely, it returned to its original approach.⁸² Finally, in the judgment of 8 November 2012 in *Commission v. Greece* the Court, on the basis of the “Baars criterion”, revised its jurisprudence yet one more time, moving back to the approach outlined in *Commission v. Italy* of 26 March 2009.

The case law is, therefore, patchy and ambiguous.⁸³

The issue is complicated by two elements: first, the absence of a Treaty definition of ‘movement of capital’; second, the potential impact that the choice of the applicable provision (freedom of establishment *and/or* freedom of capital movement) may have on the flow of investments from non-EU countries and, consequently, on the factors contributing to the growth and development of the EU’s economy.

As to the first element, the Court has held that movements of capital include both direct investments and portfolio investments.⁸⁴

Since there is no doubt about portfolio investments being a form of capital movement, the real problem lies with the notion of direct investment *vis-à-vis* that of establishment. Indeed, the fine line between the two concepts may indeed explain the shifting jurisprudence of the CJEU. More specifically, what is unclear is the difference between the direct investments covered, in the eyes of the Court, by Art. 63 (i.e., investments aimed at “establishing or maintaining lasting economic links” with a company and involving “*at least participation in the control of the entity subject of the investment*”⁸⁵) and the transactions that, according to part of the case law and based on the “Baars criterion”, are covered by Art. 49. In other words,

⁷⁷ See, for instance, *Commission v. France* of 4 June 2002.

⁷⁸ Schweitzer (2010: 103).

⁷⁹ See, for instance, *Commission v. Germany* of 23 October 2007.

⁸⁰ On the said criterion and its application also in the CJEU’s jurisprudence on golden shares see Rickford (2010: 81-93).

⁸¹ See *Commission v. Italy* of 26 March 2009, para. 39.

⁸² See *Commission v. Portugal* of 8 July 2010 and *Commission v. Portugal* of 10 November 2011.

⁸³ In these terms also Van Bekkum (2010).

⁸⁴ Generally on the topic see Hindelang (2009).

⁸⁵ Benyon (2010: 1).

it is not discernible, *stricto iure*, why direct investments, which Annex I to Council Directive 88/361/EEC defines as the “*establishment and extension of branches or new undertakings belonging solely to the person providing the capital*” and “*the acquisition in full of existing undertakings*”, should not fall within the scope *ratione materiae* of Art. 49.⁸⁶

A general application of the rules on establishment in the context of golden shares would have the advantage of eliminating right away the concerns raised by the proliferation on the European market of undesirable SWFs.

However, there are crucial political and economic reasons why, under EU law, direct investments are currently covered by Art. 63 – and here we have the second element mentioned above. The choice to opt for Art. 49 alone would, in fact, have a potentially devastating impact on investment flows, and thus affect the growth and competitiveness of the European market, insofar as it would prevent precisely the inflow of capital from third country investors, who would not be able to exercise the free movement rights conferred on them by Art. 63, but not Art. 49. However, there are also other reasons of a legal nature: the application of Art. 49 would run the risk of being in conflict with international agreements of the EU with third countries as regards the new exclusive competence provided for in Articles 206⁸⁷ and 207(1)⁸⁸ TFEU with Art. 3 TFEU⁸⁹, where the agreements themselves permit the entry of said investments into the European internal market.⁹⁰

Apart from the obvious consideration that, besides presenting a threat to the Union, the new economic-financial actors which have emerged on the international scene, as it has been already underlined⁹¹, represent important opportunities for economic growth and provide liquidity⁹², it must be stressed that, in any event, a different approach to the rules on the right of establishment would not be a solution to all the problems related to the access to the EU’s internal market of third-country investors whom EU governments regard as undesirable. At present, neither secondary law nor the case law based on Art. 54 TFEU prevent non-EU natural or legal persons from establishing companies in accordance with the law of a Member State for the purpose of enjoying the rights arising under Art. 49 *et seq.* TFEU – companies whose registered office, central administration or principal place of business is located within the Union and which, as a result, must be treated in the same way as natural persons who are nationals of Member States. Since that constitutes a circumvention of prohibitions contained in EU law, the question may thus arise as to whether, and under what conditions, the principle of abuse of law applies to the establishment of such companies.⁹³ As with all situations in which rules are evaded, what needs to be determined here is the dividing line between the

⁸⁶ See also Rickford (2010: 91-93); Torrent (2012: 548-560).

⁸⁷ “By establishing a customs union in accordance with Articles 28 to 32, the Union shall contribute, in the common interest, to the harmonious development of world trade, the progressive abolition of restrictions on international trade and on foreign direct investment, and the lowering of customs and other barriers”.

⁸⁸ “The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union’s external action”.

⁸⁹ “The Union shall have exclusive competence” in the field of “common commercial policy”.

⁹⁰ On the EU and foreign investments see, *ex multis*, Dimopoulos (2011); on this issue see *infra*, Section III.

⁹¹ See *supra*, § 1, Section I.

⁹² On the topic see Subacchi (2012).

⁹³ On the various dimensions of the said principle see Cerioni (2006) and the contributions in de la Feira, Vogenauer (2011).

indirect but legitimate exercise of the right of establishment and the deliberate circumvention of that right, which is contrary to the principles and rules of the Union.

All things considered, I would say that, despite the 'legalistic' limitations outlined above, the better option is still the adoption of the approach taken by the Court in *Commission v. Italy* of 26 March 2009 and, more recently, *Commission v. Greece* of 8 November 2012.

In any case, in order to successfully address the concerns raised by SWFs and ensure greater legal certainty, it seems desirable that the CJEU, in the absence of EU action at secondary level with regard to the capital/establishment dichotomy, should clarify once and for all the legal basis for the different types of golden shares.

2. Member States and market restrictions: socio-economic protectionism, national security and the possible application of 'old' express derogations and/or 'new' mandatory requirements.

A feasible solution for achieving a right balance between the opening and closing of the market to SWFs that wish to invest in the EU could be a statement of views put forward by the CJEU with regard to the scope of general interest exceptions to the free movement provisions in the case of non-EU State-controlled entities.

So far, the Court has not been encouraged by SWFs, by national judges, or by the European Commission to specify the scope and limits of the derogations envisaged under the TFEU, or those of the justifications the CJEU has itself provided and may consider admissible under EU law.

As to the derogations, the only provision that Member States may employ is Art. 65.1 b) TFEU, according to which national authorities have the right to "to take [restrictive] measures which are justified on grounds of public policy or public security". This is of course the case of those national measures that restrict investments in the defence and military industries.⁹⁴ More problematic is whether serious dangers for public policy and public security outside these industries may fall within the scope of the provision. I am referring to national security considerations that are strongly connected with the provision of public services, such as energy security, telecommunications, the protection of other critical infrastructures and the preservation of the control of natural resources by the host State.⁹⁵ Moreover, since there is no case law yet on the restrictions which the Member States may impose on SWF and SOE investments (i.e., case law which could help clarify the issue), an additional problem is whether the CJEU's jurisprudence on golden shares should be transposed with regard to investors in non-EU State-controlled entities. In this connection, not only has the Court maintained that, in order to be admissible, policy and security objectives must be clearly articulated and the criteria for the State intervention must be specified in objective terms; it has also stated that a restriction is legitimate and proportionate under free movement rules only when there is a "genuine and sufficiently serious threat" to public policy and public security affecting "one of the fundamental interests of society".⁹⁶

In my opinion, considering the absence of secondary legislation or a CJEU decision on the subject, at present it is not Art. 65(1)(b) TFEU, but rather an extension of the '*Cassis-Gebhard* exception' to non-EU investments that leaves room for a broader and more flexible interpretation of the requirements concerning the scope of general interest exceptions. It

⁹⁴ On this point see Chaisse (2012: 486).

⁹⁵ See Schweitzer (2011: 108-109).

⁹⁶ See, for instance, *Commission v. Spain* of 13 May 2003, paras 72-74.

seems correct to argue that one or more imperative requirements may be established in the future with respect to the entry of SWFs into the EU market: they may concern, for example, the transparency (*rectius*: lack thereof) of the operator making the investment, or whether the activity carried out by the latter is influenced by purely political interests and, thus, may put at risk the regular provision of essential sensitive activities. In that case, national measures would not have to be considered illegal merely because they provide for a regime of *ex ante* control over investments made by third country operators in privatised public utilities or public institutions in the security sector.

The result would be a distinction in treatment between EU and non-EU investors, with regard to situations which might be dangerous for the Member State that receives the investment and where the company in which SWFs intend to invest operates. In itself, this would be nothing new.⁹⁷ In its case law on taxation, the CJEU relied on both the extension of the '*Cassis-Gebhard* exception' and a flexible interpretation of the principle of proportionality, arguing in favour of a wider autonomy for the Member States and, at the same time, of stricter control over the access of specific categories of third country investors to the EU internal market.⁹⁸ The transposition of the principles set out in this area of case law to the field of golden shares is certainly desirable, since that would mitigate the concerns raised by the application of the free movement of capital to third-country direct investments by 'disreputable' operators that may possibly endanger the national as well as the EU conception of public policy, public security and public services regulation.⁹⁹ It seems therefore feasible that EU Member States may be admitted to use specific justifications to restrict the investment made by certain non EU State-controlled actors. And precisely in this consists the overlap between national and European concerns, internal market considerations and extra-commercial values, economic integration and social integration.

Moreover, a judgment of the Court in this connection would ensure that the measures adopted by the Member States in order to restrict third-country investments made by SWFs do not end up having protectionist effects¹⁰⁰ also on EU investors.¹⁰¹

III. The need for greater internal and external activism on the part of the EU in relation to SWFs: the Union as a global promoter of the rule of law and the rule of law, and the quest for a European golden share.

As is well known, insofar as the backbone of modern democracies, pluralist societies and constitutional democracies, the rule of law is one of the main values on which the EU is

⁹⁷ See the observations made by Schweitzer (2011: 103-108).

⁹⁸ See, for instance, *Orange European Smallcap Fund* of 16 June 2011, where the Court stated as follows: “[i]t may also be that a Member State will be able to demonstrate that a restriction on the movement of capital to or from third countries is justified for a particular reason in circumstances where that reason would not constitute a valid justification for a restriction on capital movements between Member States” (para. 90).

⁹⁹ See, in this regard, Art. 194 TFEU, where solidarity is put in connection with the EU policy on energy.

¹⁰⁰ As noted by the Court, the intention to target only non-EU investors was clearly expressed by the Portuguese Government in *Commission v. Portugal* (judgment of 10 November 2011, paras. 84-85) and by the Greek Government in *Commission v. Greece*, paras. 26-28).

¹⁰¹ In this regard, it seems desirable that the EU institutions clarify once and for all whether the adoption by national legislators of market access provisions that, with regard to crucial economic sectors, discriminate only against non-EU investors violates the principle of equal treatment of shareholders set out, for instance, in Art. 3 of Directive 2004/25/CE on takeover bids and/or whether it is contrary to the substantive and functional approach adopted by the Court, according to which no economic operator can be discriminated against merely on the ground of nationality, regardless of any serious public interest concerns.

founded, as recalled by Art. 2 TEU and the Preamble to the Treaty and stated by the CJEU in the famous ruling *Les Verts* of 25 February 1988.

In her recent speech on “The EU and the Rule of Law – What next?” (cited above), V. Reading, the Vice-President of the European Commission, has clarified to what extent the respect for the rule of law is a “prerequisite for the protection of all other fundamental values listed in Art. 2 TEU and for upholding all rights and obligations deriving from the Treaties”.¹⁰²

The rise of SWFs and their entry into the global market raise several concerns which directly regard the question of the respect of the rule of law by these new economic-financial actors as well as by their owners, i.e. by home States.

The EU, as underlined in § 2 of Section I, should promote good governance principles, transparency and accountability at international level, especially within the IMF and OECD.

As to the EU internal and common approach to SWFs, after dealing with the possible application by Member States of both express and jurisprudential general interest exceptions¹⁰³, I will now consider the question of whether a European golden share may be adopted by EU institutions. Now, unlike intra-EU golden shares, where two national interests clash against each other, in the context of special powers directed at limiting or even impeding the entry of SWFs the national interest overlaps with the EU interest. Here, the concerns, rather than purely national, are European.

My opinion is that the EU should (finally and) seriously assess whether a new legislation or a control mechanism with regard to non-EU State-owned investments may be enacted, inspired to a certain degree by the CFIUS US review system of foreign acquisitions of US companies, which is in place since 1975 and later amended in 1992 and 2007. In particular, with the so-called Byrd amendment of 1992, CFIUS review became mandatory for all transactions where the acquirer is controlled by or acting on behalf of a foreign government.¹⁰⁴ Even though, for obvious political and economic reasons, the approach the EU may adopt should be less strict, the result that EU institutions could achieve would be crucial since they may assess *ex ante* at the highest level the security and public policy implications of SWFs coming from non-EU countries.

Such a procedure would have the advantage of safeguarding the integrity of the single market. Indeed, individual EU countries would feel less inclined to resort to their own measures in order to erect national defences if they knew that there was a EU procedure, similar to the EU anti-dumping procedures in the common trade policy, aimed both at ensuring a common institutionalized response to the concerns raised by SWFs and at providing legal certainty to SWFs with regard to the investment regime applicable in all 28 countries. In this context, the problem of reciprocity may be dealt with by EU institutions since most SWFs are located in countries that have much more restrictive environments than the EU, as it is the case of Russia that passed a law in 2008 that limits foreign investment in 42 strategic sectors, in some cases to shares as low as 10 per cent. Obviously, reciprocity should not be applied in the strict sense or in a restrictive manner, considering the importance of SWFs for the EU economy as well as the risk of a spiral of new protectionism.¹⁰⁵

As to the problem of what would be the legal basis for an EU golden share, to my knowledge, the only possible legal basis for such a measure would be Art. 64(3) TFEU, which

¹⁰² See *supra*, footnote 27.

¹⁰³ See *supra*, § 2, Section II.

¹⁰⁴ On the US reaction to the entry of SWFs within its territory see *supra*, footnote 53.

¹⁰⁵ See Barysch, Tilford, Whyte (2008: 13).

provides for a derogation from the principle of liberalization of capitals with third countries where it is stated that “only the Council, acting in accordance with a special legislative procedure, may unanimously, and after consulting the European Parliament, adopt measures which constitute a step backwards in Union law as regards the liberalization of the movement of capital to or from third countries”. Of course, the act should be a framework directive rather than a regulation since, as known, only the former leaves the actual review processes to the member-state governments. However, the requirement of unanimity may represent a serious obstacle for the adoption of such measure, due to the existence of numerous divergences among Member States in the field. For sure, Art. 64.2 TFEU, which provides for the qualified majority in the field of capital movement, cannot be used as an adequate legal basis. Indeed, this provision applies only when the measures to be adopted by EU institutions are aimed at liberalizing rather than limiting the movement of capital to and from third countries.

Another option would be to rely on (and take advantage of) the change made by the Treaty of Lisbon with regard to the competence in the area of foreign direct investments and, therefore, also with regard to the negotiation and conclusion of bilateral investment treaties with third countries, that shifted from the member States to the EU in accordance with Articles 206, 207.1 TFEU in combination with Art. 3 TEU.¹⁰⁶

Both solutions require Member States to give up, in favour of the EU, the management and protection of interests such as national security and the protection of essential public services, interests of which they are certainly very jealous. However, in order to translate into practice the idea that the rule of law is a constitutional principle of the EU that may be applied also in the field of international trade, I believe that, as an alternative to the solution mentioned above *supra*, in § 2, Section II – centered on the application of general interest exceptions by Member States – the possibility of a major role on the part of the EU should be seriously examined, if not turned into a reality.

In conclusion, I am convinced that the quest for a fair balance between economic benefits deriving from the entry of SWFs in the EU market and the protection of national as well as European strategic/sensitive sectors must be pursued at the EU level and that, in doing so, the EU must be more *activist* and bolder.

The EU should give law a central role, regarding the market as an inherently political, institutional and social construct, rather than a self-referential *locus* that depends on its internal laws and dynamics. This seems even more urgent when market actors that, at least on paper, should be politically unbiased market-oriented investors, tend to act also as the long arm of State capitalism, that is, of foreign governments wishing to invest abroad in crucial socio-economic sectors and often connected with countries where the rule of law, in its multiple dimensions¹⁰⁷, is neither promoted nor respected.

¹⁰⁶ On the topic see, *inter alia*, Dimopoulos (2011); see also the considerations made *supra*, § 1, Section II.

¹⁰⁷ See *supra*, § 1, Section I.

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