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# The French Strategic Investment Fund: A Creative Approach to Complement SWF Regulation or Mere Protectionism?

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## INTRODUCTION

While oil-rich countries of the Persian Gulf or Asian countries with immense foreign exchange surpluses dominated the financial debates with their Sovereign Wealth Funds, France decided to launch its own, comparatively very small, Fonds Stratégique d'Investissement, in the middle of the crisis one year ago. Was it a protectionist reflex or is it rather part of a pro-active defence strategy, a way to participate in the global phenomenon of SWFs?

In a first part, I will describe and define the phenomenon of SWFs and the related concerns raised by the different involved parties, and then, in the main part, expose my favoured regulatory framework, i.e. a pragmatic approach based on current achievements by the international community on one hand and domestic regulations on the other hand. France will be particularly interesting, now that it is as well a donor country as a recipient country. Could it even be the much-sought ideal type of SWF-regulation? To conclude, I will look critically at how the French SWF was set up and how it has evolved since its inception.

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## DEFINITIONS AND CONCERNS RAISED BY SOVEREIGN WEALTH FUNDS

Sovereign Wealth Funds (SWF) are not a new phenomenon: They have been around since 1953, when the Kuwait Investment Authority, now the world's fourth largest SWF, was founded<sup>1</sup>. But they eventually caught the attention of the West around 2005, when the United States and Europe became aware that oil-rich or exporting countries from the Middle East and Asia had set up large and rapidly growing SWFs and were launching more aggressive investment strategies towards their economies. They became a source of concern when the major geopolitical actors China and Russia set up their own funds. The visibility of the SWFs reached its paroxysm in 2008, during the financial crisis, when they invested massively to save financial institutions. Since then, as we will see, there has been a shift in the strategies and in the perception of SWFs by host countries.

It is not easy to define SWFs, as there is no such thing as a typical SWF; they are all different. Nonetheless, they share certain characteristics and can be put into categories, for instance regarding the origin of their wealth (commodity exports or foreign exchange surpluses) or their purpose (stabilising funds, savings funds, reserve investment corporations)<sup>2</sup>. The International Working Group on Sovereign Wealth Funds (IWG)<sup>3</sup> defines SWFs as “special purpose investment funds or arrangements, owned by the general government. Created by the general government for macroeconomic purposes, sovereign wealth funds hold, manage, or administer assets to achieve financial objectives, and employ a set of investment strategies which include

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<sup>1</sup> Ian Bremmer, *State Capitalism Comes of Age - The End of the Free Market?*, 88 *Foreign Aff.* 40 2009, p. 44

<sup>2</sup> Martin A. Weiss, *Sovereign Wealth Funds: Background and Policy Issues for Congress*, Congressional Research Service, 15 January 2009 (cited CRS-Report).

<sup>3</sup> now renamed International Forum on Sovereign Wealth Funds

investing in foreign financial assets.”<sup>4</sup> This definition excludes operations of state-owned enterprises (SOEs), government-employee pension-funds, or assets managed for the benefit of individuals. The IWG emphasises three key-elements: (1) SWFs are owned by the general government; (2) the investment strategies include investments in foreign financial assets, thereby explicitly excluding those funds that solely invest in domestic assets; (3) SWFs are created to achieve financial objectives<sup>5</sup>. Being more precise, this definition is also narrower and the second point would exclude funds such as Malaysia’s Khazanah Nasional or, before they started investing abroad, Singapore’s Temasek Holding and Abu Dhabi’s Mubadala Development Company. Obviously, the IWG based its definition on the assumption that governmental funds do not raise particular concerns abroad if they invest only on the domestic market and, hence, do not need to be addressed by the international community.

Before the financial crisis, recipient countries evoked several concerns pertaining to the size and rapid growth of the funds, in relation with their potential macroeconomic effects and the political or geostrategic agendas of the donor countries.

As far as we can evaluate it based on published data or extrapolations, the amount of assets held by the SWFs is impressive: The aggregate portfolio managed by the SWFs is estimated between 2 and 3 trillion USD, which exceeds the assets held by all hedge funds, but is still inferior to the total assets under private management (\$53 trillion)<sup>6</sup>. The largest fund, Abu Dhabi’s ADIA is deemed to manage between \$500 and \$900 billion<sup>7</sup>. Comparing the situation before and after the crisis, Beck and Fidora expose that SWFs “would surpass official foreign exchange reserves and reach USD 7,000 billion by 2014”<sup>8</sup> and conclude that “there are no grounds to believe that sovereign wealth funds would become less important players in global financial markets in the future”<sup>9</sup>.

Despite recognised benefits, such as making the SWF’s donor country “a partner in the economic health of the host country” or potentially leading “to more open and better functioning markets within the investor nation” through encouraged reciprocity, or in particular the fostering of financial stability<sup>10</sup>, the size and growth of SWFs has raised concerns of economic nature, such as a potential distortion of asset prices in case of portfolio shifts or rumours. However, such an effect would be contrary to the theory of financial markets<sup>11</sup>, and experts agree that, overall, “the growing demand by SWFs for financial assets should be positive for the world economy”, given the fact that “SWFs typically have a high foreign currency

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<sup>4</sup> Sovereign Wealth Funds, Generally Accepted Principles and Practices, “Santiago Principles”, October 2008, p. 3 (and Appendix I, p. 27)

<sup>5</sup> Ibidem

<sup>6</sup> Trésor-Economics, No. 28, January 2008, p. 1

<sup>7</sup> CRS-Report, p. 6

<sup>8</sup> Roland Beck and Michael Fidora, Sovereign Wealth Funds – Before and Since the Crisis, *European Business Organization Law Review* 10 (2009), p. 359

<sup>9</sup> Id., p. 360

<sup>10</sup> Paul Rose, *Sovereigns as Shareholders*, 87 N.C. L. Rev. 83 2008-2009, p. 92 et seq.

<sup>11</sup> although documented in empirical literature on price pressure in financial markets, see Beck and Fidora, p. 360 et seq.

exposure, no explicit liabilities that trigger leverage or funding liquidity pressures” and that they have “a greater capacity than many other large investors to take long-term views on investments, namely to follow buy-and-hold strategies”<sup>12</sup>. Doubtless, SWFs were very helpful in recapitalising affected financial institutes, thus participating in the stabilisation of the whole banking sector. It must be underlined that it was the banks themselves who asked the different SWFs to intervene, and further that the funds are not participating in the management of the concerned banks, although their financial participations would definitely legitimise them to do so<sup>13</sup>.

Concurrently with the nascent SWF phenomenon, the Western economies were challenged by the rise of the new economic order, which allegedly entailed, besides a change in the flow of capital, relocation of businesses to lower cost-destinations, loss of jobs, and reverse-privatisations<sup>14</sup>. While SWFs do not cause this change, they are definitely part of this bigger picture. Hassan sees the root of anxiety over SWFs “in the anxiousness about the unmooring of the intellectual foundations of laissez-faire capitalism”<sup>15</sup>. He correctly highlights the “struggle about the real role of private enterprise and where should the boundaries of the state end”<sup>16</sup> and the “anxiety about the loss of sovereign power and its geopolitical consequences”<sup>17</sup>.

The concerns of political nature are due to the fact that SWFs are an investment arm of sovereign entities. Hence, unlike other investors, they could possibly be used as means to advance the political or geostrategic agendas of their governments rather than as investment devices<sup>18</sup>. Röller and Véron<sup>19</sup> identify three categories of threats potentially posed by a foreign acquisition of a US or EU company: (i) dependency upon a foreign-controlled supplier for crucial goods or services (incl. defence industry); (ii) transfer of technology or other expertise; and (iii) infiltration, surveillance, or sabotage, harming crucial areas like defence.

Such threats are not unlikely. Indeed, China’s ambitions over Africa, for example, are evident<sup>20</sup>. Moreover, Bremmer notes that the leadership of the Chinese Communist Party “dispatches China’s national oil corporations abroad to secure the long-term supplies of oil and gas that China needs to fuel its continued expansion”<sup>21</sup>. Also Russia’s endeavours are taken seriously by its neighbours such as Ukraine<sup>22</sup>. However, so far, these threats have supposedly materialised

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<sup>12</sup> Trésor-Economics, No. 28, January 2008, p. 5

<sup>13</sup> Alain Demarolle, Rapport sur les Fonds souverains, p. 12

<sup>14</sup> Gal Luft, Sovereign Wealth Funds, Oil and the New World Economic Order, in *The Rise of Sovereign Wealth Funds: Impacts on U.S. Foreign Policy and Economic Interest*, Washington DC, 21 May 2008, p. 35 et seq.

<sup>15</sup> Adnan Hassan, *A Practical Guide to Sovereign Wealth Funds*, p. 4

<sup>16</sup> *Ibidem*. See also Rose, p. 95, regarding the rise of state capitalism.

<sup>17</sup> *Ibidem*

<sup>18</sup> Rose, p. 94-96, with obvious and subtle hypothetical examples

<sup>19</sup> Lars-Hendrik Röller and Nicolas Véron, *Safe and Sound: An EU Approach to Sovereign Investment*, Bruegel Policy Brief Issue 08/2008, p. 4

<sup>20</sup> Gerard Lyons, *State Capitalism: The rise of sovereign wealth funds*, 14 *Law & Bus. Rev. Am.* 1 2008, p. 16

<sup>21</sup> Bremmer, p. 44 et seq.

<sup>22</sup> “Russia will use the economic factors to transform the internal politics of Ukraine”, said Hrigoriy Perepelitsa, director of Foreign Policy Research Institute, the academy of the Ukrainian Foreign Ministry,

not through SWFs (with the exception of Temasek and Dubai Ports World, if we consider it as extended Arm of the Dubai World fund) but through SOEs<sup>23</sup>:

- In August 2005, the Chinese CNOOC had to renounce to take control over UNOCAL because of pressures of the US authorities.
- In January 2006, Temasek had to reduce the stakeholding it aimed at in Shin Corp, a Thai media enterprise, to 42% after major uprisings had occurred in the host country.
- In May 2006, the sale of six American ports to Dubai Ports World had to be abandoned after strong reactions by Congress (although the deal had been accepted after CFIUS review).
- In May 2006, the British Secretary of State for Trade and Industry, Alan Johnson, announced a “robust scrutiny” over the bid by Gazprom over the British Centrica. The deal has not (yet) been concluded.
- In September 2006, the public Russian Bank VTB acquired 5.02% of European Aeronautic Defence & Space Co. (“EADS”), which entailed doubts by France and Germany regarding the underlying intentions. “The Russian firm was more likely pursuing political goals as well as financial goals, evidenced by a comment from Sergei Prikhodko, an aide to Russian President Vladimir Putin.”<sup>24</sup>

While there is little doubt that a SWF can exercise considerable influence over a company through a full takeover, Demarolle asks the right questions in relation with minority share stakes<sup>25</sup>: (i) Is a minority stake – especially without representative on the board – really an efficient way to achieve the above mentioned goals (especially with regard to technological and strategic transfers)? (ii) Is a SWF truly the adequate instrument for a national government, to achieve these goals? SOEs, which have the necessary experience and know-how, are much more likely to exercise influence. Furthermore, there are other (more) adequate ways to achieve geopolitical and strategic goals. Thus, it would be wrong to focus solely on the phenomenon of sovereign wealth funds while leaving aside the broader threat of foreign governments (or private firms secretly acting for foreign governments).

This being said, while the concerns were focussed on the efficient functioning of financial markets and on national security, there has been a certain shift since the financial crisis<sup>26</sup>: Indeed, SWFs are now increasingly investing in developing countries<sup>27</sup>. Today, according to the OCDE, 69% of their wealth is invested in Northern America and in Europe, but they are now investing 7 to 10% of their wealth in shares of emerging markets, i.e. an annual inflow of \$100 billion<sup>28</sup>. There is rather another concern: Western nations ask themselves how to maintain and

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quoted in Claude Barfield, Beware of Investment Protectionism, *The American* (The Journal of the American Enterprise Institute), 17 December 2008

<sup>23</sup> Demarolle, p. 12 et seq.

<sup>24</sup> Rose, p. 128

<sup>25</sup> Id. P. 13 et seq.

<sup>26</sup> Beck and Fidora, p. 365

<sup>27</sup> Lyons, p. 18

<sup>28</sup> Yves Genier, Les fonds souverains accélèrent le rééquilibrage en faveur du Sud, *Le Temps*, 27 May 2009.

attract foreign investors and in particular SWFs. Therefore they understand that they have to avoid protectionism. Hence there is a tension between open markets and protection of national interests.

## THE NEED FOR REGULATION & THE PRAGMATIC APPROACH

### 1. Why regulate the Sovereign Wealth Funds

During the last two or three decades, there was a belief in predominantly neo-liberal countries that it is best to have as few regulations as possible. However, every society, every market needs basic rules to function<sup>29</sup>. When we ask ourselves why to regulate, we must look beyond law to other disciplines<sup>30</sup>. In the ambit of SWF, we must seek on one hand what is best for the recipient country and, on the other hand, what is best for the donor country. How to define “the best”? Even within a state, there are many contradicting positions, for example between public and private interests. This renders regulation particularly complicated when several states or a whole community of nations are concerned. From a public interest perspective, regulation can be deemed necessary in case of market failures<sup>31</sup>. The financial crisis has shown us where deregulation or a laissez-faire policy can lead if nobody at all takes the initiative of regulating. Of course, a public response in the form of exaggerated regulation can have as bad consequences and, for instance, obstruct or even paralyse the economy. Public responses are requested in fields such as national security<sup>32</sup>, in order to obtain diversity, for instance in broadcasting<sup>33</sup>, or in case of irreversibility<sup>34</sup>, i.e. when the market would likely fail and lead to irreparable consequences for future generations, such as loss of know-how or extinction of endangered species. In these cases, at least at domestic level, law has a facilitating role to achieve chosen public interest objectives. On the other hand, “private interest theories of regulation are premised on an assumption that regulation emerges from the actions of individuals or groups motivated to maximise their self-interest.”<sup>35</sup> They are often linked with deregulation or self-regulation. As exposed in the regulatory space theory, “actions and intentions of regulatory actors are embedded in larger systems and institutional dynamics”. Cultural differences are reflected in the political and legal outcome. This explains why certain regulations “may involve very similar actors in different countries and yet different national political contexts would shape the preferences of those actors in different ways, leading to the emergence of different regulatory regimes”<sup>36</sup>.

On these premises, let us examine how to best address the concerns exposed in the first chapter, beginning with the recipient countries of the West. These capital-importing countries

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<sup>29</sup> Ha-Joon Chang, Ha-Joon Chang, *Globalisation, Economic Development and the Role of the State*, p. 177

<sup>30</sup> Bronwen Morgan and Karen Yeung, *An Introduction to Law and Regulation*, p. 16.

<sup>31</sup> *Id.*, p. 18

<sup>32</sup> *Id.*, p. 20

<sup>33</sup> *Id.*, p. 31

<sup>34</sup> *Id.*, p. 35

<sup>35</sup> *Id.*, p. 43

<sup>36</sup> *Id.*, p. 59 and 65 regarding national particularities

desperately need to attract foreign investments and acutely compete for it. They all recognise that “the rule of law and an appropriate degree of stability and predictability of policies form the governmental framework for domestic economic growth and also for the willingness of foreign investors to enter the domestic market”<sup>37</sup>. Economic liberalism, as defined by the Washington Consensus in the late 1980s, promising “more growth and innovation than economic protectionism within closed national or regional borders” is still the dominant theory amongst them, even though they recognise that “economic reforms need to be complemented by social and environmental policies”<sup>38</sup>. However, in reality, their economies have never been completely open or completely closed. Furthermore, there are very different policies from one country to another. Even identical words, for instance ‘protectionism’, can have very different meanings from one order to another. On the other hand, as pointed out in the previous chapter, fears regarding strategic influences sought by foreign public investors must be taken seriously. Hence there must be a well-balanced mechanism to avoid unwanted intrusion without blocking foreign investments. Blocking foreign investments can be not only harmful to the domestic economy but also, as in the case of the EU, threaten a superior order, the single market.

Sovereign wealth funds, for their part, want to access capital markets as freely as possible. Their money loses its value every day it is not invested. Therefore, they have to try to alleviate the fears of potential recipient countries, without divulging some strategies which are part of their competitive advantage over others. As an alternative, or if they are scrutinised too closely or hindered from entering a market in spite of their efforts, they can seek for more friendly jurisdictions or more interesting investments.

Donor countries, respectively their citizens whose money is being invested, also have legitimate claims. They should expect increased revenues or at least preservation of their assets, but also sound investment strategies, a good management, access to information and accountability. If their claims are not heard, they can use their political weapons, mainly electoral powers, but if necessary also, like in Thailand, public protests.

## **2. Existing regulation**

Different ways have been explored to achieve some of the regulation goals outlined above. Whereas some solutions have been elaborated at a national level<sup>39</sup>, no hard-law mechanism has been set up at the international level.

One solution would have been to regulate SWFs through a Multilateral Investment Agreement. In spite of long negotiations held under the auspices of the World Bank and the OECD and several drafts, and although there were large areas of consent, this endeavour had to be halted in 1998 because of several points of disagreement, such as the ‘*exception culturelle*’ claimed by

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<sup>37</sup> Rudolph Dolzer and Christoph Schreuer, *Principles of International Investment Law*, Oxford University Press, New York 2008, p. 11

<sup>38</sup> *Id.*, p. 79

<sup>39</sup> see below under sub-chapter 3

France and Canada in support of the French culture<sup>40</sup>. Possibly the OECD, regrouping mainly the (once) capital-exporting countries, was not the adequate forum for a question of world-importance. But then, the World Trade Organisation did not better, since its aim to include investment issues into its mandate failed as early as 1994<sup>41</sup>. Its agenda on trade issues was already complex enough.

Since multilateral options were unsuccessful, bilateral options could be explored. Whereas foreign direct investments (FDI, i.e. concrete investments in a foreign country, such as building a factory, setting up a business or a joint venture) are protected by customary international law, this is not the case of portfolio investments (mere holding of shares possibly bought on the stock exchange). The latter are usually not covered by Bilateral Investment Treaties (BITs), although there is a trend towards including them<sup>42</sup>. Hence, SOEs are more likely to be subsumed under existing treaties (which does not entail automatic approval of the investment/permission to enter the market) than funds that just buy and sell shares, even if they hold them for a certain period. BITs could be relatively easily adapted by a side-letter procedure (instead of redrafting the BIT), but this would nonetheless require distinct negotiations between donor and host states. Since every country has its specificities and given that every SWF is different, there would be endless negotiations and, in the end, no uniform practice, hence no favourable outcome for investors or investees.

Given these unfortunate non-results among states on the international level, recipient countries, acknowledging the “positive force for development and global financial stability” of SWFs, took the initiative to produce the “OECD Declaration on Sovereign Wealth Funds and Recipient Country Policies” at the OECD Ministerial Council Meeting on 4-5 June 2008 in Paris. They basically agreed, respectively repeated long-standing OECD commitments, on a voluntary, non-binding basis, that “(i) recipient countries should not erect protectionist barriers to foreign investment; (ii) recipient countries should not discriminate among investors in like circumstances. Any additional investment restrictions in recipient countries should only be considered when policies of general application to both foreign and domestic investors are inadequate to address legitimate national security concerns; and (iii) where such national security concerns do arise, investment safeguards by recipient countries should be: a) transparent and predictable, b) proportional to clearly-identified national security risks, and 3) subject to accountability in their application.”<sup>43</sup> This has to be seen as a response of the recipient countries to the voluntary framework the donor countries were setting up, and to which procedure the OECD could openly contribute.

In effect, in October 2008, the donor countries, encouraged and supported by the IMF, regulating themselves within the IWG, adopted the Generally Accepted Principles and Practices (GAPP), the so-called “Santiago Principles”. “The IWG is of the view that the GAPP, together with the OECD’s guidance for recipient countries, will help achieve the shared goal of

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<sup>40</sup> Dolzer and Schreuer, p. 26; M. Sornarajah, *The International Law on Foreign Investment*, Cambridge University Press, Cambridge 2004, p. 291 et seq.

<sup>41</sup> *Id.*, p. 27

<sup>42</sup> Sornarajah, p. 7, 8 and 227

<sup>43</sup> OECD Declaration on Sovereign Wealth Funds and Recipient Country Policies, p. 2



maintaining a stable and open investment environment.”<sup>44</sup> These principles as well represent mere voluntary guidelines, thanks to which they are more than the lowest common denominator. If they had been obliged to agree on already achieved standards or on compulsory goals, SWFs or their home countries, would not have reached a productive consensus, if any at all. But this way, there is a horizon to which the SWFs can strive. There is hope that peer pressure, acculturation and positive feedback from the recipient countries will guide more reticent funds towards the goals agreed upon, in a similar way (but without the pretention of becoming customary law) like the Universal Declaration of Human Rights, now the basis for Human Rights all around the world. In order to share gained experiences and to discuss further developments, the funds established a rather informal International Forum on Sovereign Wealth Funds<sup>45</sup>, which replaced the IWG on April 2009. Principles agreed upon include a sound legal framework to support the SWF’s effective operation and the achievement of its stated objectives (GAPP 1), clear definition and disclosure of the policy (GAPP 2), a sound and clear governance framework (GAPP 6), a clearly defined accountability framework (GAPP 10), an annual report and audited financial statements (GAPP 11 and 12), respect of all applicable regulatory and disclosure requirements of the countries in which they operate (GAPP 15). Finally, and importantly, pursuant to GAPP 19, the SWF’s investment decisions should aim to maximize risk-adjusted financial returns in a manner consistent with its investment policy, and based on economic and financial grounds. If investment decisions are subject to other than economic and financial considerations, GAPP 19.1 provides that these should be clearly set out in the investment policy and be publicly disclosed.

### **3. Pragmatic approach of SWF regulation**

My approach of SWF regulation will be a pragmatic one; it relies on the diagnosis that the nations are too diverse to be able to agree, today, on a global and binding framework to regulate foreign investments, *a fortiori* SWFs. Conversely, SWFs are too multifaceted to be governed under a detailed and compulsory international framework. Under these circumstances, the voluntary instruments provided by the OECD and the IWG are adequate, if not ideal, to alleviate concerns of capital-importing countries as well as those of investing SWFs, but they have to be complemented by national regulations. Hence, countries not adhering to the OECD Principles, for instance too protectionist states, will forgo chances of investment in their domestic economies<sup>46</sup>, whereas secretive and refractory SWFs will not be likely to operate any lucrative investment in developed countries.

The OECD Principles allow countries to set up investment safeguards in case of national security concerns, as long as they do not constitute protectionist barriers. I will compare two countries that have developed interesting systems to avoid potentially harmful foreign investments: the USA and France.

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<sup>44</sup> GAPP, p. 4

<sup>45</sup> International Forum on Sovereign Wealth Funds, <<http://www.ifswf.org/>>.

<sup>46</sup> George Stephanov Georgiev, *The Reformed CFIUS Regulatory Framework: Mediating Between Continued Openness to Foreign Investment and National Security*, p. 126, citing the example of the Sarbanes-Oxley Act of 2002 which already showed such shifts from the US to Europe and Asia.

## a) USA: CFIUS Review Process

The Foreign Investment and National Security Act of 2007 (FINSA) updated the framework established in 1975, when President Gerald Ford created the Committee on Foreign Investments in the United States (CFIUS), a body composed of different governmental agencies chaired by the Treasury. One of the goals of the reform was to address SWFs, given the growing frequency of important US assets acquisitions by these vehicles. Concerned about the disastrous precedent of Dubai Ports World<sup>47</sup>, possible backlashes in other parts of the world in case of perceived protectionism, and the competition for foreign investments pushed by other developed countries, the US had to take care to remain open to foreign investment.

The CFIUS review process starts either on recommendation from a CFIUS member agency or, most likely, with a voluntary notice from a party to a potential transaction that could harm national security. The process is fairly efficient, since the review potentially initiated by CFIUS lasts only 30 days. After this period, the committee either concludes that no threat exists and ends the review or commences a forty-five day investigation. It then sends its recommendations to the President, which may, within fifteen days, “suspend, prohibit, or order certain modifications to the transaction through a mitigation agreement, or [he] may permit the acquisition by not taking any action. Regardless of the outcome, [he] must submit a report to Congress explaining [his] decision.”<sup>48</sup> A positive feature lies in the regulatory safe harbour provided to investors once their transaction has undergone review: it is then immunised against subsequent reviews. Further, a single process allows standard treatment nation-wide. The role of Congress is increased through reporting requirements, but it cannot block specific transactions; the whole process operates within the administration. All concerned agencies and departments participate in the operations, including intelligence agencies. More problematic is the fact that FINSA does not define “national security”. There is however a non-exhaustive list of factors to consider in determining the existence of a threat to national security, i.e. among others “domestic production needed for projected national defense requirements, the control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the US to meet national security requirements (...)”<sup>49</sup>. The new list “adds the potential effects of a transaction on critical infrastructure including major energy assets; the potential effects on sales of military goods or technology to countries posing a regional military threat to the US.”<sup>50</sup> Some problems were not solved with this legislative update, such as higher transaction costs, the potential use of the process for political or own financial means<sup>51</sup>, and the necessity to address “problems arising outside of a change of corporate ownership or control”, for which there still have to be additional mechanisms to detect and remedy national security

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<sup>47</sup> Georgiev, p. 131, notes that “foreign investments in the US originating from the UAE alone fell by over \$1 billion in 2006”.

<sup>48</sup> Georgiev, p. 127 et seq.

<sup>49</sup> Georgiev, p. 127

<sup>50</sup> Id., p. 133

<sup>51</sup> Id., p. 129; Rose, p. 112 et seq.

issues<sup>52</sup>. Hence, CFIUS alone cannot resolve all possible problems caused by potentially harmful foreign investments.

## **b) France: Decree of 31 December 2005 and Economic Patriotism**

France is part of the European Union (EU) that regards FDI flows as “a crucial element for the consolidation of the internal market, while investments to and from the rest of the world ensure that the EU is well positioned in world markets and well integrated in worldwide technology flows”<sup>53</sup>. Unfortunately, the EU has not (yet?) been able to set up a system like CFIUS governing foreign investments for its whole territory<sup>54</sup>. Therefore, EU member states remain solely responsible for the assessment of national security issues. There are, nonetheless, certain provisions in the European Community Treaty and case law that are relevant to foreign investments<sup>55</sup>: They require EU member states to allow the free movement of capital, not only of investors within the EU but also of foreign investors.

“France does not have any laws or policies that specifically restrict SOEs or SWFs from investing in France.”<sup>56</sup> However, there is also an ex-ante review process, conducted by the Ministry of Economy, Finance, and Employment, in a time frame of two months. Other agencies, such as the Ministry of Defence, are asked for their inputs. The Decree, akin to FINSA, provides for mitigation through the attachment of conditions to the eventual agreement. Unlike the US, France has established a list of eleven protected sectors requiring authorisation in its Decree No. 2005-1739. Given such a precise definition of national defence and public security, France claims that its system is clear and transparent to foreign investors. Among the sensitive sectors, there are (1) gambling and casinos<sup>57</sup>, (6) production of goods or supply of services to ensure the security of the information systems, and (9) activities carried out by firms entrusted with national defence contracts or of security clauses<sup>58</sup>. However, there are several additional laws restricting foreign investments, for example in audiovisual communications and media companies (cf. the French *exception culturelle*), in the banking and insurance sector and in the aerospace sector. “Finally, a number of public monopolies exist in France that are not open to investment, including atomic energy, railway passenger transport, coal mines, gunpowder and explosives, and certain postal services.”<sup>59</sup> An important sector is missing from the lists: the energy infrastructure. Although there has been a parliamentary

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<sup>52</sup> Id., p. 129

<sup>53</sup> European Commission, Economic and Financial Affairs, <[http://ec.europa.eu/economy\\_finance/eu\\_economic\\_situation/globalisation229\\_en.htm](http://ec.europa.eu/economy_finance/eu_economic_situation/globalisation229_en.htm)>.

<sup>54</sup> For a sound analysis and a balanced solution for the EU, establishing a common framework and leaving the execution to the member states, see Röller and Véron, p. 7 and 8. See also Maaïke Okano-Heijmans and Fans-Paul van der Putten, Europe needs to screen Chinese investment, Financial Times, 11 August 2009, available under <<http://www.eastasiaforum.org/2009/08/18/europe-needs-to-screen-chinese-investment/>>.

<sup>55</sup> mainly article 56, implementing OECD principles in the EU. Pursuant to article 188C of the Lisbon Treaty, FDI will be included in the common commercial policy for which the EU will have exclusive competence.

<sup>56</sup> United States Government Accountability Office, Foreign Investment – Laws and Policies Regulating Foreign Investment in 10 Countries, February 2008 (GAO-Report 2008); Appendix VI: France, p. 59

<sup>57</sup> The EC however formally asked France to amend its Decree in 2006; discussions are still ongoing.

<sup>58</sup> GAO-Report 2008, p. 55-58.

<sup>59</sup> Id., p. 58 et seq.

motion in June 2007, there is still no relevant legal provision. In spite of this, “while the use of government golden shares is not targeted at foreign investors, the French government could use such a share to oppose any measure that might jeopardize the security of energy supplies – potentially including the purchase of French energy infrastructure by foreign state-owned enterprises, private hedge funds, or sovereign wealth funds.”<sup>60</sup> The amount of restrictions just listed above hints beyond doubt a certain economic patriotism, if not outright protectionism. But, to be fair, it must be underlined that out of 68 cases treated between 2006 and 2007, none has been refused by the Ministry and all the investors accepted the mitigation agreements proposed in slightly over 50% of the cases<sup>61</sup>. Moreover, many SWFs have already successfully invested in France<sup>62</sup>.

In his article “Globalization à la Carte”<sup>63</sup>, Sabatier marvellously illustrated the French paradox: France constantly insists on the importance of foreign investments in France, also by SWFs<sup>64</sup>, and commits itself to free trade and capital flow, but often only in one direction: French companies buy American companies (Alcatel-Lucent) and operate railways throughout the world (Connex, Veolia Transport), but when a foreign investor intends to enter the French market, there is always a reason why it is not possible in the instant case<sup>65</sup>. I agree with the authors<sup>66</sup> who recognise that economic liberalism is not absolute, that nationalist policies such as those pertaining to culture protection or industrial policy (namely with regard to the theory of irreversibility) may be justified under certain circumstances. “The question of purpose [of economic activity] is at the core of political economy, and the answer is a political matter that society must determine.”<sup>67</sup> Sabatier<sup>68</sup> quoted a poll according to which public opinion favours economic patriotism to 69%. It is hard thus, for the state, to ignore such a clear result. This explains why state capitalism has always been widely accepted in France, even by right wing politicians, as opposed to the US or other European countries that do not share France’s “protectionism”. This is also why Wintrebert<sup>69</sup>, by trying to reformulate the conditions necessary for a European protectionism, insists that the antagonism between free trade and protectionism must be qualified.

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<sup>60</sup> Id., p. 59

<sup>61</sup> Demarolle, p. 25

<sup>62</sup> Demarolle, p. 21

<sup>63</sup> Patrick Sabatier, *Globalization à la Carte*, International Herald Tribune, 8 May 2006, available under <<http://www.nytimes.com/2006/05/18/opinion/18iht-edsabat.html>>; see also Carlo Stagnaro and Alberto Mignardi, *Protectionism Will Kill Europe*, The Independent Institute, 3 April 2006, available under <<http://www.independent.org/newsroom/article.asp?id=1699>>.

<sup>64</sup> Demarolle, p. 21 et seq.

<sup>65</sup> PepsiCo-Danone; GDF merged with Suez to prevent the latter from becoming the prey of the Italian Enel.

<sup>66</sup> Robert Gilpin, *Global Political Economy – Understanding the International Economic Order*, Princetown University Press, Princetown and Oxford, p. 14

<sup>67</sup> Gilpin, p. 24

<sup>68</sup> cf. FN 63

<sup>69</sup> Raphaël Wintrebert, *Free Trade vs. Protectionism: Extricating France from a False Dilemma*, Working Paper

Under these premises, is the sovereign wealth fund established by France one year ago a creative way of complementing the existing review mechanism or is it just another protectionist device?

## THE FONDS STRATÉGIQUE D'INVESTISSEMENT

At the G7 meeting in 2007, President Nicolas Sarkozy attacked SWFs.<sup>70</sup> One year later, he set up the French-style SWF<sup>71</sup>: The Strategic Investment Fund (SIF).

The SIF was created in the middle of the global downturn in order to support the development of small and mid-cap enterprises with a strong potential for innovation and sector leadership, and to stabilise the capital companies deemed strategic to the French economy (i.e. those possessing specific know-how, key-technologies, jobs of national importance, and in general the automobile, aerospace, shipbuilding and railway industries). It was endowed with EUR 20 billion, i.e. 14 billion worth of stakes in French companies, previously held by the government and the Caisse des Dépôts et Consignations (CDC), and 6 billion of cash. The fund is owned by CDC (51%) and the French government (49%).

Although it is definitely sovereign, in the sense of government owned, and even strategic, the SIF is at odds with the definition of SWFs exposed at the very beginning of this paper. Firstly, France did not have any surpluses that it wanted to manage separately from the central bank; but at least the fund owns major French companies, the same way Temasek owns SingTel, Singapore Airlines or the banking group DBS. Secondly, and most importantly, contrary to the definition of the IWG expressly excluding funds not investing abroad, the SIF aims uniquely at investments on the domestic market. As such, and in consideration of its relatively meagre resources, it does not pose any (hypothetical) concerns to other recipient countries. This is not to say that the SIF does not raise any concerns at all on its domestic market: The main concern is certainly the one of protectionism; it can also affect competition, for instance if it acquires shares to a price exceeding market prices or if the SWF has some insider knowledge, e.g. through state intelligence; finally, if the management is deficient or investments are not planned carefully, the fund could face bankruptcy and would have to be held accountable to its constituents, the French citizens. Therefore, the SIF does after all combine both aspects: the one typical to donor countries and, through the fears of protectionist behaviour, the one typical to recipient countries. Thus, it is appropriate to call the SIF an SWF, as Sarkozy wished from the beginning.

When he created it, Sarkozy insisted on the fact that it should be a model, exactly following the guidelines recipient countries would want to impose upon SWFs. Is this goal close to be achieved? The legal framework that established the fund is not to be questioned: The fund is constituted as a French public limited company (société anonyme, SA), and updated articles of

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<sup>70</sup> “We’ve decided not to let ourselves be sold down the river by speculative funds, by unscrupulous attitudes which do not meet the transparency criteria one is entitled to expect in a civilised world. It’s unacceptable and we have decided not to accept it.”, quoted in Larry Elliott, Darling backs G7 move on sovereign funds, *The Guardian*, 19 October 2007

<sup>71</sup> Speech of 20 November 2008 at Montrichard. It contains the whole strategy and organisation.

incorporation are readily available<sup>72</sup>. The global structure of the fund, as a subsidiary of CDC, a long-established service company of the French state, is clear, the governance model is exemplary and takes into account French specificities: There is a Board of Directors composed of 7 members (2 representatives of CDC, 2 of the state, 3 other qualified persons), chaired by a president (the director of CDC), including an investment committee (presided by the manager of the fund); it is directed by a Directeur général; and finally, to guarantee coherence and a balance in the fund's strategy, there is a Comité d'orientation, comprising representatives of the economy, of labour unions (of utmost importance in France, to avoid strikes and public protests), and other qualified persons. Though being run by the state, the SIF is independent from the government; but since the government shares the citizens's views on state capitalism, views enforced by the SIF, there is a factual link between these parties. Parliamentary oversight is guaranteed by the Commission de surveillance of CDC (composed of 5 Members of Parliament), which has been a grant of independence of this organism since 1816. Since the fund's scope is not in the first line to maximise revenues but strategic, it had to be clearly set out in the investment policy and be publicly disclosed, pursuant to GAPP 19.1. This has been done: The fund's strategy was publicly announced by the President and has been refined later in a publicly available document<sup>73, 74</sup>.

This being said, everything is not yet perfect. Parliamentary interventions and a free press can and do help guiding the fund: At first, the SIF has been criticised for turning away from the stated strategy, namely in some "firemen's actions". It has also been criticised for not being socially responsible enough, i.e. investing in firms that would undergo restructurings in spite of the state's help (in the case of Nexans). Heads of trade unions have complained that, in spite of their unions being members of the Comité d'orientation, they struggle to receive substantive information. Despite the published strategy, the regular press releases, the financial statements (to be published) and the oversight mechanism, Members of parliament wish even more transparency and a reinforced exterior supervision. The Norwegian fund is cited as a good example for parliamentary cooperation. The FSI, for its part, rejects these allegations as unsubstantiated, recalls the intense parliamentary supervision and the fact that it has merely minority shareholdings, but admits that it is still very young and that it can evolve and become even more respected<sup>75</sup>.

Turning to the recipient side, we note that within a year of its inception, the SIF has directly invested EUR 450 million in 14 companies and further 650 million in different regional and sectoral partnerships. The economic choices have been embraced so far<sup>76</sup>.

Finally, concerning the fear of protectionism, the fund does not seem to reinforce the existing barriers. Admittedly, its size does not allow it to compete with SWFs of the Middle East. But interestingly, since its foundation, the SIF appears to be very open to cooperations with foreign

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<sup>72</sup> Fonds Stratégique d'investissement, Statuts, Mis à jour le 15 juillet 2009

<sup>73</sup> Les orientations stratégiques du Fonds stratégique d'investissement, 20 April 2009

<sup>74</sup> Sénat.fr, Le fonds stratégique d'investissement, un "fonds souverain à la française"?, 16 January 2009; Fonds Stratégique d'Investissement, <<http://www.fonds-fsi.fr/>>

<sup>75</sup> Marie Visot, Le fonds souverain français grandit dans l'ombre, Le Figaro, 21 Octobre 2009

<sup>76</sup> Id.

investors, notably SWFs. To this end, it had contacts to many SWFs and concluded a Memorandum of Understanding with Mubadala<sup>77</sup>, deemed as complying with the international expectations, for future joint investments. France would remain in charge of the operations and make sure that its domestic strategic goals are achieved, whereas Mubadala would benefit from its investments and from a new level of legitimacy.

This kind of collaborations has been saluted by international observers who view them “as a sign that SWFs are maturing into more sophisticated investors; cognizant of their limitations and looking for the tools to overcome them. This in turn (as Waki suggests<sup>78</sup>) will contribute to SWF’s international acceptance.”<sup>79</sup>

## CONCLUSION

France has a tradition of state capitalism, which is not totally compatible with the EU’s liberal view on the common market and foreign investment. However, the fund it created, while being an instrument of economic patriotism, cannot be accused of increasing France’s insulation from the globalised world. To the contrary, through the Fonds Stratégique d’Investissement, France participates in the “select club” of SWF donor countries and, through cooperations with other funds, can really be a player, even a trend setter.

Together with a CFIUS-like foreign investment review mechanism, to be established on EU-level to achieve the greatest efficiency, smaller French-style SWFs can truly achieve the goal of good regulation.

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<sup>77</sup> FSI / Mubadala, <<http://www.fonds-fsi.fr/fr-fr/les-partenaires/le-fonds-mubadala.html>>

<sup>78</sup> Natsuko Waki, Sovereign funds join forces for strategic investment, 18 August 2009, <<http://uk.reuters.com/article/idUKTRE57H3C820090818>>.

<sup>79</sup> Ashby Monk, Cooperation Begets Commercial Success, 18 August 2009, Oxford SWF Project, <<http://oxfordswfproject.com/2009/08/18/cooperation-begets-commercial-success/>>.

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