DOING BUSINESS IN ROMANIA; FOREIGN DIRECT INVESTMENTS (FDI);

TRADING ENTITIES –INVESTMENT MECHANISMS; PROTECTION SYSTEM; GUARANTEES [1]

Corina Cristina BUZDUGAN, PhD,

Elena Mihaela FODOR, PhD,

Rodica Diana Apan, PhD

Christian University "Dimitrie Cantemir" Bucharest,
Facultaty of Law, Cluj Napoca,Romania

Abstract

The present study focuses on a number of essential features of foreign direct investments (FDI). The first part of the study indicates illo tempore the judicial landmarks of the state's policy on FDI, in the context of economic policy and in connection to the landmark regulations in the field, from 1990 up to the present. This part also explains the investment mechanisms now traditional in the field of FDI, namely companies, subsidiaries or their branches. One of the most relevant principles in setting up companies, expanding their activity at the European Union level and developing FDIs is that of the freedom establishment on the territory of another Member State, other than the state of the national. In determining the law applicable to the organic statute of the company as well as to subsidiaries and branches set up in Romania by the national from another Member State, their nationality must be established, which relates to their registered office. If the determination of their registered office is rigorously

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established through existing regulations at the national level, the determination of the real office, whose landmarks for regulation are not clearly determined, may attract uncertainty concerning the law applicable to the organic statute of the company and its dismemberment.

The second part of the study elaborates the protection and guarantees, those shared by foreign and Romanian investors as well as those of the foreign investors alone. This part casts a targeted look at the interdiction instituted ex lege by the nationalisation, expropriation or other measures having an equivalent effect on the FDI, excepting the cases where the requirements of the law are met, as well as on the foreign investor's right of choice regarding the entities and procedures that may be applied for the resolution of potential disputes between him and the Romanian state, concerning rights and obligations of parties involved in an FDI relationship.

Keywords: *foreign direct investments, investment mechanism, protection system, guarantees*

JEL Classification: L21, M2, E32

1. COMPTE RENDU OF THE REGULATIONS IN THE FIELD OF FOREIGN DIRECT INVESTMENTS (FDI) IN ROMANIA;PERSPECTIVES ON THE INVESTMENT MECHANISMS FOR TRADING COMPANIES UNDER LAW 31 OF 1990

The investment attractiveness of Romania as host state and of its business environment having in view the essential features regulated *illo tempore* in order to facilitate and encourage foreign investments in Romania are revealed by the doctrine(Ilie, 2012, p.349-354).

One first regulation in the field of foreign investments in Romania was decree-law 96/1990 on certain measures to attract foreign investment in Romania published in the Official Gazette no.37 of 20/03/1990. In order to carry out foreign investments there needed to be set-up trading companies with foreign participation either in association with Romanian legal or natural persons or with full foreign capital. The trading company would gain legal personality on its registration with the Minister of Finance. The regulation esteblished also the

facilities to be granted to foreign investors, which consist of exemption from corporate tax for 2 years after first earning taxable revenues. Decree-law 96/1990 was abrogated once a new more extensive regulation in the field of FDI was passed in the form of Law no.35/1991 on the regime of foreign investments, published in the Official Gazette no.73 of 10 April 1991, republished in the Official Gazette no.185 of 2 August 1993, hereinafter called Law no.35/1991.

In brief, Law no.35/1991 regulated certain signifiant components in relation to FDI, which afterwards are to be traced as guidelines in following regulations in the field, namely in GEO 31/1997 on the regime of foreign investments in Romania, published in the Official Gazette no.125 of 19 June 1997, hereinafter called GEO 31/1997, as well as in GEO 92/1997 concerning incentives for foreign direct investments, published in the Official Gazette no. 386 of 30 December 1997, consolidated version on 1 January 2007, hereinafter called GEO 92/1997 in force at the moment.

Thus, the regulated guideline provided by art.4 of the GEO 92/1997 are basically the following: - guarantees against nationalisation, expropriation, or similar measures with equivalent effect; - customs and fiscal advantages; - assistance with the administrative procedures; -right to conversion from Lei into foreign currency of the revenue gained from the invested amount, as well as the transfer of currency to their country of origin, in accordance with the provisions on currency regime; - investors' right to choose the competent law or arbitration courts in case of disputes; - the possibility to report the loss registered during a fiscal year on the profit to be registered in the following fiscal years; - the possibility of accelerated amortisation; -the possibility of deducting the advertisment and publicity expenses from taxable profit; - the possibility of hiring foreign citizens in compliance with legal provisions in force. The doctrine (Căpățînă, 1991, pp.5-26 andPătulea, 1993, pp. 2-20) offers an extensive analysis of the evolution of regulations in the field of foreign investments as well as those provided by Law 35/1991.

Under Law 35/1991 and as revealed by the doctrine (Capatana, 1991, p.13) the legal investment mechanism for FDI is non-restrictively represented by the setting-up or expanding trading entities through new branches and subsidiaries having full foreign capital or in association with legal or natural Romanian persons, their regime being regulated by the provisions of Law 31/1990 on trading companies, published in the Official Gazette no.126 of 17 November

1990, consolidated version of 1 February 2014, hereinafter called Law 31/1990 and the formalities required to register a company, subsidiary or branch in order to carry a FDI in Romania are provided by Law 31/1990 and by Law 26/1990 on the trade registry, published in the Official Gazette no.121 of 7 November 1990, consolidated version of 1 February 2014, hereinafter called Law 26/1990.

The traditional investment mechanisms in the field of FDI are companies or their subsidiaries or branches which are regulated under GEO 31/1997 and GEO 92/1997. GEO 31/1997 reinforces the role of companies stipulated by Law 31/1990 as investment mechanisms, in that it non-restrictively provides the means by which the foreign investment can be carried out in Romania, one of the means being the participation of a foreign investor with consideration in cash represented in freely convertible currency, as well as with in-kind capital, to the formation of the share capital of a trading entity, Romanian legal person as well as the participation to the expansion of the such trading entity or indirectly to one of its subsidiaries.

GEO 92/1997 defines the concept of„foreign direct investment" as being the *participation to the formation or expansion of an enterprise under any of the forms provided by the law,* acquiring shares or capital of a trading company, except for the portofolio investments, or *set-up and expansion in Romania of a foreign company subsidiary by one of the following means:* -consideration in cash represented in the national currency or in a freely convertible currency, - in-kind capital in the form of immovable and movable property, tangible and intangible; - participation to the growth of a company's assets by any means of financing, and the doctrine (Navasardyan, 2012, p41-58) undertakes a comparative analysis of the way in which the concept of foreign investment is perceived by the legislation of various different states amongst which Romania as well.

Companies, subsidiaries and branches that represent investment mechanisms are regulated as indicated above, by Law 31/1990 even where these are carried out by setting-up or expanding a company by the national of a Member State other than Romania. Out of all the investment mechanisms stipulated by GEO 92/1997, the investment mechanisms indicated *ut supra* are located and determined by the moment of the set-up or expansion, considering that in the present analysis the expansion comprises restrictively the set-up of a subsidiary or branch.

In the field of company law one of the most relevant principles applicable to the expansion of the activity of companies at European Union level and the development of FDI is that of the freedom of establishment, provided by art.49 of the TFEU (former art.43 TCE). The principle of the freedom of establishment provides this freedom for the nationals of a Member State acting on the territory of another Member State, including the set-up and governance of companies in accordance with the provisions laid down by the host State for its own nationals – the host state also institutes restrictions with regard to the establishment of agencies, branches or subsidiaries by the citizens of a Member State. The principle of the freedom of establishment is developed in the doctrine (Sandru, 2014, p.11-40) especially analyzing of the evolution of the EUCJ case-law in the field, in cases: Centros C- 212/97; Uberseering C 208/00; Inspire Art C 167/01; Servic Sistem C 411/03; Cartesio C -210/06; Vale C -378/10, analyzed also in Oprea (2011).

With the above principle as corollary, the foreign investor national of a Member State, may choose the investment mechanism to be employed in order to carry out economic activity on the territory of another Member State, Romania as host state in this case, from a number of possibilities amongst which are the following: (i) setting-up a company in any of the types of doing business restrictively regulated by Law 31/1990 namely: a) general partnership, b) limited partnership, c) limited partnership by shares, d) limited liability company, e) joint-stock company; (ii) setting-up branches or subsidiaries by a company operating on the territory of another Member State. Both hypothesis share a noticeable aspect for the investment activity, which due to its relevance for the accuracy of the investment environment and the protection of investors' interests is represented by the law applicable to the company and to the subsidiaries and branches set-up by the national of another Member State in another Member State, in this case Romania.

Law 31/1990 provides in art.1 the principle of the freedom of associationin view of carrying-out profit-making activities by legal and natural persons who may set-up companies with legal personality, in accordance with its provisions, and para.2 establishes the principle to apply when determining the citizenship of a company in relation to its registered office.The consequence of this principle is that the companies having the registered office in Romania acquire Romanian citizenship, irrespective of the capacity of nationals of another Member State of the persons setting it up, as the national law – Romanian is applicable for these

companies. The scope of the national law is determined by the provisions of art. 2581 of the NCCR,the new Civil Code in force since 01.10.2011,hereinafter called NCCR, article which together with art.2581 cited below are part of the regulations of Book II „International Private Law Regulations".

In accordance with these provisions – art.2581 of the NCCR, the law of the organic statute of the legal person rules mainly: a) the capacity; b) the means of acquiring and losing the capacity of associate; c) the rights and obligations of associate; d) method to be used for the election or appointment of the legal person's managing body, their competence and functioning; e) governing bodies of the legal person; its representation through their own authorities; f) the liability of a legal person and her bodies towards a third party; g) the modification of the constitutive acts; h) the dissolution of a legal person.(The statistical data available on the site of the National Trade Register Office http://www.onrc.ro/index.php/ro/statistici?id=254, accesed on 11.03.2015, p.22 table 21 and chart no.9 reveal the number of registrations of companies with foreign share capital and the evolution of the number of companies between 1991 and 2014, the higer peaks being in 1994 – 11.053 registrations and 2007 -15.720 registrations, while in 2014 were registered 6.619 companies. On the other hand, the applicable law to the stage of the set-up of companies that represent investment mechanisms for the FDI, named „foreign participation companies", according to art.286 of Law 31/1990, is precisely this law, also making reference to the law regulating the regime of foreign investments, in so far as this law regulates certain aspects concerning the set-up.

Regarding the subsidiaries and branches of the company, Law 31/1990 provides in art.44 the freedom of the foreign companies to set-up in Romania, complying with Romanian law, subsidiaries, branches, agencies, representativea or other secondary offices, as long as this right is recognized by the law of their organic statute. Hence, the law regulating the set-up of subsidiaries, branches, agencies, representatives and other secondary offices is enforced in the form of Law 31/1990, however there isn't enforced a law applicable to these secondary offices following their set-up. The doctrine, (Bodu, 2014, pp. 82-83; Sitaru,2013,pp.539-599 and Oprea, 2011) reveals the scope of art.2580 (2) (3) of the NCCR in determinig the law of the organic statute of the subsidiary and the branch set-up in Romania by the legal person national of another Member State. While the organic statute of the legal person is governed by its national law, in accordance with art.2580 (1) of the NCCR with reference to previously

cited provisions of art.2581 of the NCCR, the organic statute of the subsidiary set-up in another country falls under the applicability of that country's national law, and respectively, the organic statute of the subsidiary falls under the law of the state where it has its own registered office, irrespective of the law applicable to the legal person that set it up.

But in determining the citizenship of the company there is also the regulation on the principle of the real registered office, developed by the doctrine (Bodu, 2014, p.84- 87), with special view on the risks posed by its enforcement (in Sitaru, pp.163-169 and in Oprea, 2011 who reveals the complications that may arise in practice, when applying this principle). Hence, in accordance with the provisions of NCCR, art.2571 (2), where there are offices in several states, the determining element in identifying the citizenship of the legal person is the real office. This is defined, in accordance with art.2571 (3) of the NCCR, as being the office where there is the main governing and managing center, even if the decisions of the respective body are adopted according to the guidelines transmited by shareholders or associates from other states.

Consequently, if the criterion for determining the citizenship and thus the applicable law according to the registered office of the company, subsidiary, branch established by the regulations in force in Romania, has rigurously mapped landmarks, the reference to the criterion of the real office, whose regulated landmarks are not clearly mapped, may generate in certain cases ambiguity in the investment environment in Romania, more as the EUCJ case-law analyzed in the doctrine (Sandru, 2014, p.11-40 and Oprea, 2011) did not adopt a unitary direction on the criterion of the real office.

Therefore, taking in consideration the expansion of the companies and their tendancy to seek means of benefiting from exemptions, especially of fiscal nature, the determination of the real office, different from the registered office, may in practice attract uncertainty regarding the law applicable to the organic statute of the company and its dismemberments, a statute that comprises a series of defining elements for the foreign investor such as: the means of acquiring and losing the capacity of associate; the rights and obligations of the associate; the functioning of the governing body. This leads to the conclusion that one of the primary landmarks regarding which foreign investors are to be „guided" at the time of the investment in Romania, shall be the principle of the law appli-

cable in what concerns the registered office and the consequences of the bifurcation between the registered office and the real office.

2. PERSPECTIVES ON THE PROTECTION OF GUARANTEES GRANTED TO FOREIGN INVESTORS IN ROMANIA

The guarantees offered by the Romanian legal framework for FDI cover the key points of the case of any relationship between foreign investors and the host state: protection against discrimination, protection against expropriation which is not of public interest and which otherwise would not be fairly compensated, protection against unfair treatment , protection of capital transfer. Regarding the ownership right the law regulates the means of acquiring it, the stability of the right and access to justice. The Constitution of Romania guarantees and protects the ownership right irrespective of the holder of the right, through the provisions of art.44 (1) (2), the content and limitations of the right are established by the law.

The guarantees are strengthened by the provisions of art.136 (5) according to which private ownership represents an intangible right under the organic law. Special legislation in the field of FDI, respectively GEO 92/1997 on incentives for the stimulation of direct investments, provides in art.6 that a trading company legal persons, resident or non-resident may acquire any real rights over real estate, providing that the estate is necessary for carrying out the activity of the legal entity and must comply with the social object set forth in the constitutive documents and with the legal provisions on acquiring private ownership right over land by foreign citizens and nationals as well as by foreign legal persons. Presently, the conditions necessary for acquiring ownership right over land by foreign citizens and foreign legal persons are regulated by Law no.3012/2005, and GEO no. 184/2002 regulates the special right to use the land within incorporated area, purchased by foreign citizens and foreign legal persons as well as the possibility to convert it in a ownership right.

Constituional guarantees offered to ownership right refer to nationalisation and expropriation. The Constitution of Romania adopted in 1991 made reference only to expropriation, in the provisions of art. 41 (3). In this context, the Constitutional Court of Romania, following a pre-promulgation control of the

law on the regime of free areas, through Decision no.4/1992 declared unconstitutional the provision according to which investments carried out in free areas could not be nationalised, but for cases of public interest, and in compliance with the legal provisions and only providing the prompt, adequate and effective payment of compensation equivalent to the value of the investment. This decision shows that in the absence of the constitutional provision that would establish nationalisation as a means of forced transfer of goods from private ownership into state's public ownership, through the order of the competent state authority, results the constitutent's will to eliminate this means of ownership transfer on reason that it is interpretable and raises suspicion on the cause why it is enforced and possibly leading to abuse from public authorities. Subsequently however, GEO 92/1997 on the stimulation of direct investments made reference again to nationalisation in art.4 (2) (c) providing that investors in Romania benefit from guarantees against nationalisation, expropriation and other such measures having equivalent effect. The provisions on nationalisation can currently be considered as complying with the Constitution, as through the revision of the supreme law in 2003 the content of art.41 that became art.44 after republishing, was completed with the provision of para.(4) which interdicted nationalisation and any measures of forced transfer of goods into public ownership on grounds of social class, ethnical, religious, political membership of the holders.

The express mention of nationalisation as method of ownership transfer is the result of a more complex understanding of this term. In the period close to 1990 when there was a switch of political regime, Romania entering in the group of democratic states, nationalisation was perceived as an abusive seizure of property, without granting compensation, such as it was applied by the communist regime. Afterwards the perception changed and nationalisation became accepted in the way it is applied in democratic states (Kuisel, 1981, 272-279; Einaudi, 1950, 177-191). Hence in nowdays nationalisation is by principle not permitted and cannot be disposed but in exceptional cases and under the conditions provided by art.8 (1) of GEO 92/1997 that is in cases where it is necesary for public interest reasons and it is carried out in accordance with the express provisions of the law and only provided the previous payment of adequate effective compensation.

Looking closer at this last guarantee, paragraph (2) of the same article mentions that compensation shall be equivalent with the real market value of the

expropriated investment assessed right before the expropriation or before the iminent expropriation becomes publicaly known and affects the value of the investment. Investor protection is complemented by access to judicial authority or to any independent and competent authority in accordance to the international treaties Romania adhered to, as far as the legal character of the measure is concerned as well as regarding the assessment of the investment or payment of compensation, possibility guaranteed by paragraph (4) of the same art.8.

Expropriation is regulated also as an exceptional possible means of ownership transfer for public utility grounds. Regarding the specificity of FDI, case Saluka Investments B.V. c. Czech Republic, FDIS Tribunal showed that in accordance with international law, a legal measure adopted on public grounds and which amongst other affects also a foreign investment is not considered as having the character of expropriation and is not offsetting, except for the case where the government granted specific commitments to the potential foreign investor, who at that time regarded making investment. Guarantees against unfair treatment from the state are similarly granted in the case of nationalisation, in the same content of the Constitution and of GEO 92/1997. Expropriation however benefits from more developed legal framework, the provisions of Law 33/1994 on expropriation for causes of public utility, provides detailed administrative procedures to be carried out previously to the declaration of public utility, expropriation, compensation assessment and payment. The law provides the possibility of retrocession of the expropriated good if within a year the expropriated real estate have not been used for the purpose declared in view of expropriation, or if the works have not begun. These provisions underline the protection of the ownership right in accordance with the interpretation given by the European Court of Human Rights art.1 of Protocol no.1 of the European Human Rights Convention, which Romania ratified through Law 30/1994. This case-law is thus applied directly by the national judge, granting protection against certain expropriations.

In a case where the urban nature of an area was changed by the local city council as a result of an investment plan for the contruction of a highway, a plan that was suspended afterwards for economic reasons, the Court of Apeal of Cluj –department for administrative, fiscal and commercial disputes, through final Decision no. 420/2010 established that under the current conditions of uncertainty regarding the future use of the land for public interest, the refuse to allow the owner of a land that is affected by the respective local urban plan, to

raise a building on its land represents an infringement of the ownership right, which does not make justice to the requirement of proportionality (Brumărescu c. României, para. 78), and that the state did not fulfill its obligation to ensure the effective exercise of the right of ownership conffered by art. 1 of Protocol no.1 of the Convention, thus breaking the „fair balance" that must exist between the requirements of public interest and the requirements for protection of the owner's rights (Păduraru c. Romania para. 112). The theoretical recognition of the owner's right to exercise thei right of use and dispose of its goods, without practically existing the possibility to exercise these rights is the equivalent of an actual infrigement of the ownership right (Sporrong si M. c. Suedia). The decision is not the only one of this kind in Romanian case-law.

The legal limitations over the ownership right are provided by the Civil Code. They are established either for the protection of private interest relating to the use of natural running waters, temporary works and distances required for certain construction, works and plantations, view over the neighbouring property, right of way, right of way for utilities (articles 602-630); The works in the field of mining and petrol extraction or electrical energy are regulated by special provisions (Diaconu, A.M., 2011, 65-75). The legal limitations for public interest of administrative and economic nature are provided in art.586, 587 of the Civil Code.

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