CLIFFORD
CHANCE

Briefing note May 2014

Reinforcement of the French foreign investment control: Back to protectionism?

In the wake of high-profile acquisition projects announced in the French telecom, energy and transportation sectors, a controversial new Decree relating to foreign investments in France has just been released on May 15, 2014.

Decree n°2014-479 of 14 May 2014 reinforces the control of the French Minister of Economy over so-called "sensitive foreign investments" in France. In particular, it extends the material scope of its control to six new strategic sectors, i.e., energy, water, transport, electronic communications and health and infrastructures of vital importance. The Minister of Economy's powers are also slightly extended.

Given the impact of this procedure on their transactions, foreign investors need to anticipate this regulatory constraint at an early stage of the process and be prepared to address it.

Decree n° 2014-479 dated May 14, 2014 reinforces the existing foreign investment control. The material scope of the foreign investments which are subject to prior approval from the Minister of Economy is broadened and the Minister of Economy's powers in this context are adjusted, and even extended to some extent.

Pursuant to the French foreign investment control regime (Articles L.151-3 and seq. and Articles R.153-1 and seq. of the French Monetary and Financial Code ("CMF")), foreign investments in so-called strategic sectors are subject to a prior approval from the Minister of Economy. Once filing is complete, the Minister of Economy has two months to make a decision. Failing this, the investment is deemed authorized.

Where applicable, this foreign investment control procedure means that a transaction cannot be closed until after the issuance of this prior approval. "Jumping the gun" is sanctioned by criminal (seldom applied) and administrative fines. In addition, any contract pursuant to which the investment concerned is directly or indirectly made is deemed void.

The types of foreign investments subject to prior approval are the following:

- Investments made by a non EU/EEA investor which consist of: (i) the acquisition of control of a company with headquarters in France or (ii) the acquisition of all or part of a business branch of a company with headquarters in France or (iii) crossing the threshold of 33.33% shareholding or voting rights in a company with headquarters in France, provided that the target company or business is active in a strategic sector.

- Investments made by a EU/EEA investor which consist of (i) the acquisition of control over a company with headquarters in France or (ii) the

acquisition of all or part of a business branch of a company with headquarters in France, provided that the target company or business is active in a strategic sector.

In addition, acquisitions of all or part of the business division engaged in a strategic sector of a company with headquarters in France made by a French registered company, which is itself controlled by a company with headquarters located outside France, may also be subject to the same prior authorization regime as the aforementioned investments.

The most remarkable changes to the existing regime brought by Decree n°2014-479 ("the Decree") will be addressed below.

1. Six new sectors are added to the list of strategic sectors (Articles R.153-2, R.153-4 and R.153-5-2 CMF)

The extension of the list of strategic sectors is certainly the most controversial provision of the Decree in light of the current context, i.e., the pending takeover of Alstom by GE which appears to be concerning for the Government.

Under the previous regime, eleven sectors[1] are classified as strategic. With the exception of gambling, they primarily relate to national security and defence interests.

Six new sectors have now been added to this list by the Decree, i.e.:

- Energy supply (energy, gas, oil or other energy source) ;

- Water supply ;

- Operation of **transport** networks and services ;

- Operation of electronic communications networks and services (**telecommunications**) ;

- Operation of a facility, installation or structure which are of vital importance within the meaning of Articles L. 1332-1 and L. 1332-2 of the French Defence Code ;

- Protection of **public health**.

These new sectors are applicable to both non-EU foreign investments, investments from the EU and EEA and investments made by a company constituted under French law but controlled by a foreign person or entity.

2. The scope of the commitments is broadened (Article R.153-9 CMF)

The minister may give his approval subject to commitments being made by the foreign investor.

These commitments may pertain to the preservation by the investor of (i) the sustainability of the activities, (ii) industrial capabilities, (iii) R&D capabilities or associated knowledge, (iv) the security of supply or (v) the performance of the contractual obligations of the company headquartered in France.

What are the changes?

- The (non-comprehensive) list of the types of commitments, which reflected the national interests included in the previous list of strategic sectors, has been broadened in order to be consistent with the broadened material scope of the control (no specific reference is however made to the water sector).

- The power of the Minister to require foreign investors to divest an activity to a third party has been extended. Previously, the Minister could just impose the divestment of an ancillary activity falling within a strategic sector. Now, the Minister may order the divestment of any activity falling within the scope of the strategic sectors. It means for instance that even if the activity represents a very significant part of the targeted business or company, foreign investors may be forced to divest it. This could be a way for the Minister of Economy to kill a project, without having to rule against it.

3. The grounds for refusal are adjusted to the new sectors (Article R.153-10 CMF)

The circumstances under which the Minister of Economy may validly refuse to grant his authorization were broadly defined as follows: (i) a serious presumption that the investor might commit criminal offences, (ii) the fact that commitments cannot suffice to preserve national interests, (iii) the sustainability of the activities, the industrial capabilities, the research and development capabilities and the associated knowledge could not be preserved as a result of the investment, (iv) the security of supply could not be guaranteed, or (v) the performance of the contractual obligations of the company, which has its headquarters in France, as holder or subcontractor of public procurement contracts could not be guaranteed.

A first addition concerns the cases

[1] When the investor is headquartered in a EU/EEA Member State, the sector list is less extensive.

Key issues

- The material scope of the French foreign investment regime has now been extended to energy, water, transport, electronic communications, infrastructures of vital importance and public health and the Minister of Economy's powers have been slightly extended.
- Given the impact of this procedure on their transactions, foreign investors need to anticipate this regulatory constraint at an early stage of the process and be prepared to address it.
- Even if it remains to be seen how the Decree will be applied in practice, one may reasonably expect that it will be applied in a sensible and pragmatic way by the French authorities, as the application of the Decree will be closely monitored by the EU Commission.

referred to in (v) above: public procurement contracts related to 'public order' are now also included.

In order to reflect the enlargement of the material scope of the control, the Decree also amends the reference to the security of supply. It adds references to cases where the integrity, security and continuity of supply of (i) a facility, installation or structure of vital importance, (ii) transport networks and services, (iii) electronic communications and (iv) public health, cannot be guaranteed. No specific reference is made to the water sector though.

4. What are the practical consequences for foreign investors willing to invest in France?

A first consequence of this revision is that the question of the potential controllability of a transaction within the meaning of the foreign investment regime will have to be raised more often as the material scope is now broadened.

This is even truer when one considers the vagueness of the wording of the Decree in relation to these new sectors, which confers a large discretion on the French Minister of Economy.

There is indeed a risk that in practice the latter be tempted to opt for a broad interpretation of the material scope, although the fact that the criminal nature of the regulatory requirements should in principle lead to a narrow interpretation.

Safeguards appear rather limited: if foreign investors have in principle the right to challenge the French Minister of Economy's binding decisions before the administrative judge, very few of them (not to say none) actually enforce their right. Foreign investors have indeed shown so far little appetite for potentially lengthy litigation against the French State, the outcome of which is always uncertain. But this may well change if the French State does not apply the Decree in a reasonable way.

Only a handful of cases have hence been challenged thus far before the national judges and the case-law in this field is therefore almost non-existent.

Such situation creates legal uncertainty to the foreign investors' detriment. It is made all the more so by the fact that the consultation procedure, which allows a foreign investor to request a comfort letter from the Minister in case of doubts on whether a transaction would fall under the Decree, is not practicable. The Minister has up to two months to respond to such a request and is not obliged to do so. Moreover, the absence of response within this period does not exempt foreign investors of their duty to notify.

In case of doubts, it is thus generally more efficient to directly request a prior approval, and insert a condition precedent in the contractual documentation accordingly.

A second consequence is that it puts foreign investors at higher risks both in terms of potential commitments and rejection of the file.

But one may reasonably expect that these increased risks will concern only the most politically sensitive foreign investments.

If it is very frequent that commitments are imposed to foreign investors, they can be negotiated with the State and may be more or less burdensome depending on the sensitiveness of the activities concerned.

In practice, the cases where the prior approval is refused have been so far very rare.

A third potential consequence of this revision will be an increase in complexity of the cases and in the duration of the informal phase of the procedure (i.e., before confirmation of the completeness of the filing and

hence before the clock of the two month period starts ticking). The procedure traditionally gives rise to inter-ministerial services consultation as the latter act as instructing services (e.g., defense ministry for defense related investments, environmental and defense services for energy). Due to the enlargement of the scope of sectors, other ministries (e.g. health ministry) will now have their say. Besides, it cannot be excluded that the increase in the number of filings resulting from the revision will be a source of additional delay in the treatment of the files, and thus impact the timing of the transactions. It will thus be crucial for foreign investors to reach out to the Treasury at a very early stage of their project in order to pave the way to a smooth process, or, in more sensitive cases, well identify any hurdles the project may face.

Despite the negative impression conveyed by the Decree, it clearly remains to be seen how it will be applied in practice. One may reasonably expect that only highly political files will be at risks in terms of potential reinforced commitments and potential rejection.

In any event, we remain hopeful that the Minister of Economy will opt for a sensible and pragmatic approach to this revision.

5. What does the future hold for this Decree?

This reinforced control over foreign investments will certainly give rise to extensive and lively discussions between the French authorities and the EU Commission, which has already expressed some concerns and stated that it will carefully monitor the compatibility of the revised regime with EU law.

One may say that it has an after-taste of *déjà vu*. In 2006, the EU Commission launched an infringement proceeding against France in relation to its foreign investment control regime because the then applicable regime encroached on the free movement of capital and the freedom of establishment[2]. The infringement proceeding however never reached the contentious stage before the European judges.

It can neither be excluded that the Decree be challenged before the national courts.

---

[2] EU Commission's press release of 12 October 2006, IP/06/1353.

Contacts

Patrick Hubert
Partner
+33 (0) 1 44 05 53 71
patrick.hubert@cliffordchance.com

Thierry Schoen
Partner
+33 (0) 1 44 05 52 47
thierry.schoen@cliffordchance.com

Gilles Lebreton
Partner
+33 (0) 1 44 05 53 05
gilles.lebreton@cliffordchance.com

Marie-Laure Combet
Senior Associate
+33 (0) 1 44 05 51 46
marie-laure.combet@cliffordchance.com