

GERMANY FOLLOWS THROUGH WITH TIGHTER CONTROLS ON FOREIGN DIRECT INVESTMENT

Following the salient *Leifeld* decision, the German government steps up the game by lowering the acquisition threshold for review, making foreign investments more difficult. Investors should be aware of the risks involved.

LEIFELD DECISION AS TRIGGER

Earlier this year, the planned acquisition of the German company Leifeld Metal Spinning, a manufacturer of mechanical engineering products, by Yantai Taihai, a private undertaking based in China, was the first ever deal to be formally authorised for prohibition by the German government. This was due to concerns that sensitive know-how and technology may be transferred to China which could be used for military purposes. Back then, this seemed to be the culmination of an ongoing development towards greater scrutiny of foreign direct investments ("FDIs") into Germany.

Yet, flowing from the ensuing discussions and continuing concerns, the latter resulting also from other cases in particular from the energy sector, the German Federal Ministry for Economic Affairs and Energy (*Bundeswirtschaftsministerium*, "BMW") adopted amendments to the Foreign Trade and Payments Ordinance (*Außenwirtschaftsverordnung*, "AWV"), mainly subjecting even more deals to its review. The amendments are expected to come into force at the beginning of 2019.

THE IMMINENT CHANGES

Under the current legal framework, the BMWi may prohibit the acquisition of domestic targets if the deal is thought to endanger the "public order or security" of the Federal Republic of Germany. At the same time, such powers are restricted to deals by which the buyer acquires at least 25% of the voting rights in the target, in particular where the target operates a critical infrastructure (cross-sectoral investigation), or where the target is active in certain defence-related areas (sector-specific investigation).

First of all, the amendments will lower the relevant threshold for review from currently 25% down to a mere 10% threshold, at least in the context of the operation of critical infrastructure (applying to non-EU investors) and insofar as the sector-specific investigation (relevant for non-German investors) is concerned. From the BMWi's perspective, this is meant to reflect that even a lower stake in an undertaking could under certain circumstances amount to decisive influence.

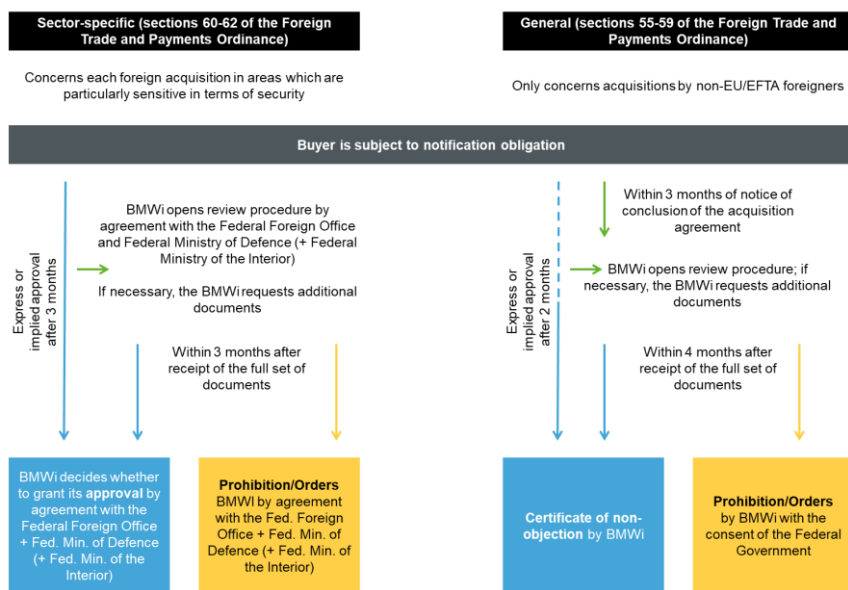
Key issues

- Policy shift towards greater scrutiny of FDIs to continue
- Threshold for review lowered from 25% down to 10% for operation of critical infrastructure and defence-related investigation
- Expansion of the scope of application of AWV to media undertakings

Secondly, the scope of application of the AWV will be extended to undertakings active in the media sector. The 10% threshold will apply to media undertakings as well.

Finally, in contrast to the BMWi's proposed initial amendments, the ultimate ordinance passed by Cabinet does not further specify the starting point from which the review period begins to run. Instead, the review period continues to be delayed if the BMWi – or indeed any other ministry involved in the process – requires additional documents or has further questions. As a result, the amendments miss out on the chance to simplify the procedure and to create greater certainty in the process.

Review of company acquisitions ≥ 10 %



There is still more on the horizon, though. In light of a looming agreement concerning a European framework for investment control, there is a high likelihood of further amendments impending. In particular, it is expected that the AWV will adopt the European framework's scope of application, as a result of which the AWV's own scope of application would be extended significantly compared to the status quo.

PRACTICAL CONSEQUENCES

The practical implications of the amendments cannot be predicted with certainty. However, it can be assumed that the amendments to the AWV will likely lead to an increase of the number of notifications to be submitted to the BMWi.

Further practical implications are subject to the BMWi's application of the new legal framework. The BMWi has a rather wide discretion and it remains to be seen how this discretion will be exercised in particular cases. Guidelines which could provide for greater legal certainty in this respect are not available. In addition, the review process is not free from political influence which makes it even less predictable.

In summary, the importance of FDI scrutiny in Germany will certainly increase following the amendments to the legal framework. This could apply all the more depending on the outcome of the BREXIT negotiations.

CONTACTS



Marc Besen
Partner

T +49 211 4355 5324
E marc.besen
@cliffordchance.com



Dr. Dimitri Slobodenjuk
Counsel

T +49 211 4355 5943
E dimitri.slobodenjuk
@cliffordchance.com

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Clifford Chance, Königsallee 59, 40215
Düsseldorf, Germany

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