

CORONAVIRUS: NEW BARRIERS TO FOREIGN DIRECT INVESTMENT IN SPAIN

Spanish Royal Decree-Law 8/2020, of 17 March, on urgent extraordinary measures to address the economic and social impact of COVID-19 (the "RDL") has suspended, effective as of 18 March 2020, the regime on the deregulation of foreign direct investment in Spain, indefinitely, until the Spanish Government decides otherwise. It has added a new Article 7 bis for this purpose and has established new rules on sanctions in Articles 8 and 12 of Act 19/2003, of 4 July, on the legal regime governing the movement of capital and financial transactions with foreign countries. The RDL is based in this regard on Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union ("**Regulation 2019/452**"), and reproduces some of its provisions practically word for word.

The consequence of this suspension will be that it will now be necessary to first obtain an administrative authorisation from the State in order to be able to make these investments in Spain.

In practice, the aim of this regime is to supervise the acquisition of Spanish companies by investors from non-EU countries or countries not signatories to the European Free Trade Agreement, with a view to avoiding what the Government could consider to be opportunist acquisitions of listed and unlisted Spanish companies whose equity value is being reduced.

Key issues

- Do these measures in the RDL apply to investments from any foreign countries?
- Does the new regime of administrative authorisation have a limited duration?
- What is foreign direct investment?
- Does it affect foreign direct investment in any activity?
- What sectors are considered strategic and require administrative authorisation?
- Is authorisation required when the company's participation in these sectors is minimal?
- What other foreign direct investment requires administrative authorisation?
- Does it affect transactions already in progress?
- Do investment transactions performed without authorisation have any effect?
- Should this authorisation be obtained prior to the authorisation for a potential takeover bid by the CNMV?
- What is the period established for the Administration to decide on the authorisation?
- Do these rules replace other foreign investment control regimes?

1. DO THESE MEASURES IN THE RDL APPLY TO INVESTMENTS FROM ANY FOREIGN COUNTRIES?

No, because investments from European Union countries, Norway, Iceland, Switzerland and Liechtenstein are not considered foreign direct investment, for this purpose.

During the Brexit transition period, the United Kingdom will retain the status of Member State of the European Union, pursuant to Article 127.6 of the Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community. This transition period ends on 31 December 2020, although it may be extended by one or two years.

2. DOES THE NEW REGIME OF ADMINISTRATIVE AUTHORISATION HAVE A LIMITED DURATION?

In principle, it will be in force indefinitely.

However, as the reason that has led the Government to establish this regime is linked to the fall of value of Spanish companies as a result of the COVID-19 crisis, which represents a clear threat of acquisition of such companies by foreign investors (literally copying what the Preamble of the RDL says), the Government has reserved the possibility of cancelling this measure at any time, by means of a resolution.

3. WHAT IS FOREIGN DIRECT INVESTMENT?

For the specific purposes of these new measures adopted by the RDL, this means investment by residents of countries outside the European Union and the European Free Trade Association, when the investor comes to hold a stake equal to or greater than 10 per cent of the share capital of the Spanish company, or when as a result of the corporate operation, act or legal transaction it gains effective participation in the management or control of said company.

In this regard, it should be specified that:

- a) It only applies to investments in companies and not to other transactions such as asset purchases.
- b) In our opinion, if by means of any kind of agreement or concerted transaction with third parties, the possibility to effectively participate in the management or control of the company were acquired, jointly, this regime would apply, even if the foreign investor does not reach 10% of the capital of the company.
- c) Authorisation is also required for indirect investments that allow the investor to acquire control of 10% of share capital or effective participation in the management or control of the company. Even though the RDL does not expressly state as much, the Supreme Court, in its Judgment of 4 March 2013, on the occasion of the application of the regime of foreign investment in Spain in activities directly related to national defence, concluded that it also applied to indirect investments in which the end investor controlled the acquired company.

Meanwhile, Article 2.1) of Regulation 2019/452 defines the concept of *"foreign direct investment"* very broadly (*"an investment of any kind by a foreign investor aiming to establish or to maintain lasting and direct*

links between the foreign investor and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity in a Member State, including investments which enable effective participation in the management or control of a company carrying out an economic activity"), meaning that it includes indirect controlling stakes.

In fact, the Preamble of Regulation 2019/452 highlights this possible problem, stating that "*Member States that have a screening mechanism in place should provide for the necessary measures, in compliance with Union law, to prevent circumvention of their screening mechanisms and screening decisions. This should cover investments from within the Union by means of artificial arrangements that do not reflect economic reality and circumvent the screening mechanisms and screening decisions, where the investor is ultimately owned or controlled by a natural person or an undertaking of a third country.*"

4. DOES IT AFFECT FOREIGN DIRECT INVESTMENT IN ANY ACTIVITY?

No. Although the RDL considerably increases the scenarios in which authorisation for foreign direct investment is necessary, it applies not only to investment in companies that operate in the strategic sectors defined in the RDL (which correspond largely to those envisaged in Regulation 2019/452), but also to investment in other sectors, when the investor is in any of the objective circumstances contemplated in the RDL that make it necessary to obtain prior authorisation (also matching those envisaged in Regulation 2019/452).

The Government reserves the possibility to extend this regime to other sectors, when public security, public order or public health may be affected.

5. WHAT SECTORS ARE CONSIDERED STRATEGIC AND REQUIRE ADMINISTRATIVE AUTHORISATION?

- a) Critical infrastructures, whether physical or virtual (including energy, transport, water, health, communications, media, data processing or storage, aerospace, defence, electoral or financial infrastructures and sensitive facilities), as well as land and properties that are key for the use of such infrastructures, understood as those contemplated in Act 8/2011, of 28 April, which establishes measures for the protection of critical infrastructures.
- b) Critical technology and dual use products as defined in Article 2, section 1, of Council Regulation (EC) number 428/2009, including artificial intelligence, robotics, semiconductors, cybersecurity, aerospace, defence, energy storage, quantum and nuclear technology, as well as nanotechnology and biotechnology.
- c) Supply of essential produce, energy in particular, understood as that which is regulated in the Act 24/2013, of 26 December on Electricity Sector, and Act 34/1998, of 7 October, on the Hydrocarbons Sector, or those referring to raw materials, as well as food safety.

- d) Sectors with access to sensitive information, personal data in particular, or with the ability to control such information, in accordance with Organic Act 3/2018, of 5 December, on Personal Data Protection.
- e) Communications media.

As you can see, the list of sectors is indeed lengthy.

6. IS AUTHORISATION REQUIRED WHEN THE COMPANY'S PARTICIPATION IN THESE SECTORS IS MINIMAL?

Yes, the RDL does not establish a distinction, even if it may seem disproportionate on some occasions.

7. WHAT OTHER FOREIGN DIRECT INVESTMENT REQUIRES ADMINISTRATIVE AUTHORISATION?

Those in which any of the following scenarios arise:

- a) if the foreign investor is directly or indirectly controlled by the government, including the public bodies or armed forces, of a third country (outside the European Union or the European Free Trade Association -Norway, Iceland, Switzerland or Liechtenstein-), with Article 42 of the Commercial Code applying for the purposes of determining the existence of such control.
- b) if the foreign investor has made investments or participated in activities in sectors that affect security, public order and public health in another Member State, strategic sectors in particular.

In our opinion, will be difficult to determine in some cases whether the activity of the investor in other activities in another Member State affect security, public order and public health, unless it is in one of the strategic sectors.

- c) if administrative or judicial proceedings have been brought against the foreign investor in another Member State or in the State of origin or in a third State due to the commission of criminal or unlawful activities.

8. DOES IT AFFECT TRANSACTIONS ALREADY IN PROGRESS?

The new regime applies to foreign direct investment "performed" or "carried out", according to the terminology used by the RDL. For that reason, it will apply to those transactions in which the effects of the investment have not yet materialised. In other words, those operations in which only signing has taken place will have to obtain the administrative authorisation required by this RDL.

However, as the reason for approval under the new regime is to supervise foreign investments relating to the acquisition of Spanish strategic companies whose value has fallen as a result of the COVID-19 crisis, it does not make much sense to require that authorisation for transactions that have already been signed, and are just pending execution. It is something that is a matter for debate.

9. DO INVESTMENT TRANSACTIONS PERFORMED WITHOUT AUTHORISATION HAVE ANY EFFECT?

Investment transactions carried out without the mandatory authorisation will be null and void, devoid of any legal effect, unless they are legalised by obtaining the corresponding authorisation, notwithstanding any sanctions that may apply.

10. SHOULD THIS AUTHORISATION BE OBTAINED PRIOR TO THE AUTHORISATION FOR A POTENTIAL TAKEOVER BID BY THE CNMV?

Yes, because this authorisation must be subject to the regime envisaged in Article 26.2 of Royal Decree 1066/2007, of 27 July, on the regime for takeover bids for securities.

11. WHAT IS THE PERIOD ESTABLISHED FOR THE ADMINISTRATION TO DECIDE ON THE AUTHORISATION?

Once the application for authorisation is submitted, it is for the Government to grant or refuse it, within a term of six months. A failure to issue a decision by the end of that term will be deemed a refusal.

12. DO THESE RULES REPLACE OTHER FOREIGN INVESTMENT CONTROL REGIMES?

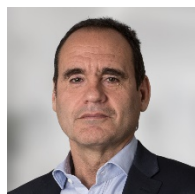
No, under no circumstances. It will be necessary to comply with the additional foreign investment control regimes in certain scenarios, such as in relation to investment in activities directly related to National Defence, or regarding the acquisition of holdings in energy companies, among others.

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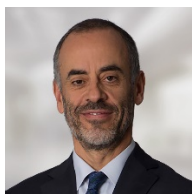
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