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Foreign Direct Investment

# Foreign Direct Investment: An overview of the EU and national case law

FRANCE, GERMANY, UNITED KINGDOM, ITALY, SPAIN, REGULATORY, MERGER NOTIFICATION, FOREWORD, EUROPEAN UNION, THRESHOLDS, CHANGE OF CONTROL, REFORM, FOREIGN INVESTMENT, MINORITY SHAREHOLDINGS, COMPETITION POLICY, COVID-19

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It's a well-established fact: investment screening mechanisms have existed for a long time. The introduction of such rules, which allow governments to scrutinise individual investment proposals for their potential impact on essential security interests, can be traced back to the 1960s in some countries. Nevertheless, many countries were historically relying on single-sector authorisation requirements or similar mechanisms at most. Therefore, in practice, foreign direct investment ('**FDI**') screening mechanisms had rather limited implications on transactional practice areas and mainly concerned investments in the defence sector.

In recent years, we have seen the arrival of a new wave in FDI policymaking. FDI compliance has now become a top priority for investments within the European Union ('**EU**') for a broad range of sectors, defined as critical infrastructure (energy, transport, water, health, communications, media, data processing, or storage, aerospace, defence, electoral or financial infrastructure, sensitive facilities, and crucial real estate) and critical technologies (AI, robotics, cybersecurity, energy storage, nuclear technologies, nanotechnologies, and biotechnologies).

Following the outbreak of the Covid-19 pandemic, this trend has increased. Attempts to protect domestic businesses and to secure access to medicine and medical equipment have sparked a return to protectionism.

Much water has passed under the bridge since e-Competitions' last Special Edition on Foreign Investment in December 2020 [*1*]. This foreword provides an overview of the developments in FDI regimes globally during 2021 and, more specifically, (1.) highlights the trends over the year in the EU and (2.) in a number of key EU Member States together with the UK, (3.) with an added focus on the reasons why FDI screening increasingly matters [*2*].

## 1. EU trends: National competence, European cooperation

Since the EU Foreign Direct Investment Screening Regulation (Regulation 2019/452 or the "EU FDI Regulation") entered into force on 10 April 2019 and applied to transactions from 11 October 2020 onwards, there has been an increasing trend amongts Member States towards reforming foreign investment to shield strategic industries and businesses from opportunistic acquisitions by "foreign" investors [*3*].

The power to screen FDI remains firmly in the hands of national authorities, nevertheless the EU FDI Regulation establishes a framework for screening foreign investment by EU Member States. The EU FDI Regulation allows the European Commission to review certain investments of 'Union interest' (though the Commission has no direct power to block investments under the FDI Regulation) and to issue a non-binding opinion to the Member State in which the investment is intended to be made.

Whilst the Covid-19 pandemic has intensified consideration of this issue, there had already been a move by national governments to tighten foreign investment controls prior to the global outbreak. As a matter of fact, the list of EU Members States with no FDI screening mechanism has been decreasing rapidly over the last few years. At the time of writing, eighteen EU Member States plus the UK are reported to have screening mechanisms in place [*4*], with a further four Member States considering measures [*5*]. A minority of four other Member States neither have, nor have any plans to implement an FDI screening regime [*6*].

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This obligation to exchange information is part of the cooperation mechanism established under Regulation 2019/452 but is subject to strict rules on confidentiality as it concerns the security or public order of one or more Member States or the functioning of an EU project or program relevant for the security of the EU as a whole. Screening undertaken by the Member States is indeed confidential and the EU cooperation mechanism, therefore, respects the same rules. Lack of confidentiality would make it difficult to share sensitive information which is essential for meaningful cooperation. Therefore, the Commission does not publicly disclose any information be it related to individual FDI transactions or to the screening of any FDI transaction nor to any opinion issued on any given FDI transaction. However, the Commission intends to publish an annual report about the implementation of the Regulation, which will be based on annual reports submitted by the Member States to the Commission. The first annual report is expected to be adopted after the summer of 2021.

This focus on "coordination and cooperation" between Member States is of paramount importance as it sets the minimum standards for national regimes and likely heralds an increasingly harmonized and robust screening of FDI in the EU.

The European FDI cooperation mechanism is also relying on a standard-form template that Member States are encouraged to use when notifying an FDI under the cooperation mechanism [*7*]. Published in April 2021 after six months' experience, the European Commission, at the initiative of DG TRADE, has developed this template notification form aimed at gathering relevant, specific and targeted information. The purpose of the form is to enable a faster assessment by the Commission and Member States under the cooperation mechanism of whether an FDI undergoing screening is likely to affect security or public order in at least one other Member State. In practice, it allows the other 26 Member States and the European Commission, when receiving and examining a notification pursuant to said cooperation mechanism, to obtain standardised information to assess the impact on their security and public order and on programs and projects of Union interest for the European Commission.

The logic behind this form is that by upgrading the quality of information within the cooperation mechanism, one speeds up its examination by the remaining 26 Member States and the European Commission and enables the notifying Member State to finalise its investigation without delay.

As a follow-up, on 5 May 2021, the European Commission proposed new legislation to take measures against market-distorting subsidies from foreign governments [8]. This is an attempt to address a perceived failure of public procurement and trade defence mechanisms under current EU antitrust, merger control, state aid law and even national FDI regulations. Under this legislation, the Commission would be empowered to intervene in takeovers of EU companies or public procurement bids when they are supported by state subsidies from third countries. In particular, it would create a new filing obligation and would give the Commission exclusive competence to assess the existence of distortive foreign subsidies in transactions and public tender bids. In practice, the proposed legislation would introduce an obligation for companies that have received foreign subsidies to notify M&A deals and bids submitted in public procurement procedures. This proposal for a Regulation on foreign subsidies distorting the internal market will be submitted to the European Parliament and Council, which will have to approve it before it can be implemented, a process not expected to be concluded before late 2022.

## 2. National trends: Tightening the foreign investment net

Changes are happening quickly as governments seek to protect critical industries without deterring foreign investment more generally.

In particular, over the last few months, several Member States have reviewed their screening mechanisms, or adopted specific new mechanisms to cover investments in new sectors such as healthcare and biotechs. Other countries, such as France, Italy or Spain, adopted temporary regimes to ensure the protection of their national interests in the aftermath of the Covid-19 pandemic.

In France, the French government tightened its control by extending until 31 December 2021 the lowered 10% threshold for screening non-EU investments in listed French companies that were put in place during the Covid-19 pandemic and which was due to expire at year-end 2020. In addition, the French Minister of Economy publicly tightened its position as it issued two negative decisions over the last few months that made headlines even if such formal vetoes remain extremely rare. In the context of the interest shown by the American Teledyne in the French company Photonis, specialised in night vision systems, the French Ministry at first verbally opposed any agreement, before discussions continued throughout summer 2020. The discussions had reached a point where the following conditions were imposed by the Ministry, (i) the taking of a 10% minority stake in Photonis by the French sovereign investment fund Bpifrance, accompanied by a veto right regarding the operations and management of Photonis’ European businesses in France and the Netherlands and (ii) the establishment of an internal security committee including representatives of the French Ministry of the Armed Forces and the French Ministry of the Economy and Finance, who would not only have veto rights but would also filter information in order to limit the transfer of strategic data to Teledyne. Nevertheless, ultimately those discussions came to an end with the formal prohibition by the French State at the end of last year. The other negative decision was issued more recently, in January 2021. The French Ministry of Economy vetoed Canadian retailer Couche-Tard’s buy-out of Carrefour, in the name of French food sovereignty, illustrating the topicality of control of foreign investments. For dealmakers, those veto decisions set the high-water mark in a rising tide of protectionism and are a signal of stronger protection of French companies from non-European investors, even for close economic partners of France such as the United States or Canada.

In Germany, following several changes to German foreign investment rules in 2020, the German Ministry for Economic Affairs and Energy (Bundeswirtschaftsministerium) continued tightening the German FDI net and published a 17th amendment to the German Foreign Investment Regulation (Außenwirtschaftsverordnung – "AWV"), which came into force on 1 May 2021 [9]. Under the new rules, 16 additional industries have been included in the AWV’s scope. In addition, further types of transactions, e.g. increase of existing voting rights exceeding certain thresholds or the acquisition of certain corporate governance rights, are subject to foreign investment scrutiny as well. Those recent changes follow an ongoing trend in Germany whereby the German Authority has demonstrated its mounting willingness to step in and protect what it perceives to be its national interests. Indeed, end of last year, on 2 December 2020, the German government prohibited the acquisition of German company IMST GmbH, Kamp-Lintfort, by a Chinese investor. This was the second high-profile prohibition decision issued by the German government under FDI regulation [*10*].

In Italy, new notification requirements were introduced following the Covid-19 pandemic and are intended to remain in force until at least 31 December 2021. They cover EU investors acquiring control over companies in certain sensitive sectors (other than defence and national security) and non-EU investors acquiring 10% or more of the capital of entities identified as strategic pursuant to a recent Prime Minister's Decree which entered into force on 14 January 2021 (D.P.C.M. 179/2020). The Decree extended the scope of Italian FDI regulation provided that the overall value of the investment is equal to or greater than EUR 1 million.

In Spain, among the many measures that the Spanish Government has adopted as a result of the declaration of the state of emergency, one that stands out was the transitional rule that was initially implemented until 30 June 2021 (and which has since been extended until 31 December 2021) which requires authorisation to be obtained for certain investments by residents of other EU and the European Free Trade Association ('EFTA') countries. This is an additional regime additional to the one introduced during the first state of emergency in 2020 for investments by non-EU/EFTA residents. In Spain, the need for authorisation for foreign investment is now the norm, when it had previously only been required exceptionally, for very specific sectors, when carried out by residents of countries outside the EU and EFTA [*11*].

Last but not least, the UK government has been catching up with its international peers. Whilst the UK has had a public interest regime in force for nearly twenty years, the UK Government could only intervene on national security grounds in deals that fell within the scope of the UK's merger control regime (and under the jurisdiction of the UK Competition and Markets Authority) and investments in the defence sector. The UK Government announced on 20 July 2021 that the substantive provisions of the new National Security and Investment Act [*12*] is expected to enter fully in force on 4 January 2022. The Act will introduce a framework that requires mandatory notification and approval for acquisitions of shares above 25%, 50%, and 75% in entities in certain sensitive sectors. The definitions of the 17 sensitive sectors (which are still in draft) are also quite broad, which allows a range of investments to be caught. The government will also have the right to call in for review on national security grounds acquisitions of material influence over either assets or shares in any sector for up to 5 years from completion, including where deals complete after 12 November 2020 but before full commencement of the Act, such that voluntary notifications might be appropriate in certain cases.

## 3. FDI has featured increasingly on the radar for cross-border M&A

Whilst a few years ago, FDI screening had limited implications for M&A transactions as its impact was generally limited to investments in the defence sector or in critical infrastructure, foreign investment control has now become a major issue in M&A transactions, introducing a new dynamic of negotiation with investors. As with merger control, the risk of a foreign investment control review is no longer an exception and must be taken into account both in terms of the certainty of the transaction and of the timing of its completion. In this respect, the due diligence stage now plays a key role in securing foreign investment issues given even low minority shareholdings can trigger the application of FDI rules, as can contractual arrangements, other rights, and acquisitions of assets.

When planning an M&A transaction, FDI filings need to be considered alongside competition-based merger control rules. In addition, parties should bear in mind that governments have a greater degree of discretion under FDI regimes for making substantive interventions compared to other regulatory processes, as FDI regulatory reviews are more at risk of politicisation. There is also generally less transparency, with fewer publicly available precedents, and less guidance. The result is a degree of uncertainty that needs to be factored into the overall deal risk. This means that the parties may need to seek prior authorisation, as early as the due diligence phase, and to treat the need for such prior authorisation as a condition precedent to the completion of their contractual arrangements. In practice, a preliminary multi-jurisdictional analysis will need to be carried out in order to identify the various jurisdictions likely to apply foreign investment control and to impact the global transaction, very much as parties do for screening their merger control obligations.

Since, under the existing FDI regimes, Member States have powers to ban certain investments or ask for mitigating measures, if it is established that an investment is likely to affect security or public order, it is now even more critical to anticipate the FDI risk in cross-border M&A transactions.

As with other regulatory approval requirements, where a transaction falls under one or more FDI regimes, there will be implications for the deal timetable. Reviews can take a number of months and, where transactions are subject to mandatory prior notification, this will prevent closing of the transaction even in circumstances where there are no substantive national security concerns. Early engagement on potential FDI notification obligations can help to mitigate the impact.

Given the aim of governments to preserve domestic capacities and prevent what they consider to be predatory acquisitions, investors should consider early in the process whether there are specific assurances or commitments that they might be willing to offer in appropriate circumstances. These might, for instance, include maintaining domestic production capacity; protecting domestic R&D; maintaining domestic jobs.

Where time is of the essence, parties may need to structure the transaction such that the deal can go ahead with certain parts of the target held separate in those countries where more time is needed from an FDI point of view.

**Note from the Editors: although the e-Competitions editors are doing their best to build a comprehensive set of the leading EU and national antitrust cases, the completeness of the database cannot be guaranteed. The present foreword seeks to provide readers with a view of the existing trends based primarily on cases reported in e-Competitions. Readers are welcome to bring any other relevant cases to the attention of the editors.**

[*1*] See ***Christian Ahlborn, Christoph Barth and David-Julien dos Santos Goncalves***, *Foreign investment: An overview of EU and national case law, 17 December 2020, e-Competitions Foreign Investment, Antitrust Case Laws e-Bulletin, Art. N° 98126.*

[*2*] We are grateful for the contributions by our colleagues Dimitri Slobodenjuk, Caroline Scholke (Germany), Laura Tresoldi (Italy), Carme Briera (Spain) and Chandralekha Ghosh (United Kingdom) to this article.

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[*3*] See also *https://www.cliffordchance.com/briefings/2020/10/eu-foreign-investment-screening- regulation -takes-effect—a-high-.html*.

[*4*] DG Trade maintains an up-to-date list of Member State schemes at *https://trade.ec.europa.eu/doclib/docs/2019/june/tradoc_157946.pdf*. Amendments to the Swedish Protective Security Act (Sw. Säkerhetsskyddslagen) entered into force on 1 January 2021 and these changes establish a screening system concerning the sale of certain security-sensitive activities. Since the new screening system specifically targets activities that are sensitive to Swedish security interests, it should be considered narrower than a FDI screening mechanism which would target FDI more broadly.

[*5*] Belgium, Estonia, Ireland, and Luxembourg.

[*6*] Bulgaria, Croatia, Cyprus, and Greece.

[*7*] See *https://trade.ec.europa.eu/doclib/docs/2021/april/tradoc_159530.pdf*.

[*8*] See ***Merit Olthoff, Vanessa van Weelden, Andreas Von Bonin****, The EU Commission publishes the results of its consultation on foreign subsidies, 23 September 2020, e-Competitions September 2020, Art. N° 97798 and see* ***Jay Modrall****, The EU Commission adopts a proposal for a regulation to combat distortions of competition caused by subsidies granted by non-EU states, 5 mai 2021, e-Competitions May 2021, Art. N° 100780* ; ***Françoise Labrousse, Bernard Amory, Renato Antonini, Charles de Navacelle, Kaarli Harry Eichhorn, Eva Monard****, The EU Commission adopts a proposal for regulation on foreign subsidies that might be distorting the internal market, 5 May 2021, e-Competitions May 2021, Art. N° 100983* ; ***European Commission****, The EU Commission adopts a white paper on foreign subsidies in the single market, 17 June 2020, e-Competitions June 2020, Art. N° 95506.*

[*9*] The latest amendments extend the mandatory filing requirement to 16 additional industries increasing the number of sensitive sectors from 11 to 27, including certain areas of earth remote sensing systems, artificial intelligence (AI), autonomous driving or flying, industrial robots, semiconductors, cybersecurity, aeronautical/aerospace, nuclear technology, quantum technology, additive manufacturing (3D printing), network technologies, smart meter gateways, information and communication technology, critical raw materials, secret patents and agricultural real estate. See also : *https://www.cliffordchance.com/briefings/2021/05/german-foreign-investment-control-tightened-again---may-2021.html*.

[*10*] See ***Peter D. Camesasca, Horst Henschen, Martin Juhasz,*** *The German Government prohibits the acquisition of a telecommunication company by a Chinese buyer under the foreign direct investment rules (IMST / Addsino), 2 décembre 2020, e-Competitions December 2020, Art. N° 98214* ; ***Falk Schöning, Sebastian Faust, Stefan Kirwitzke****, The German Government prohibits the acquisition of a communications technology company by a Chinese communication product manufacturer (IMST / Addsino), 2 December 2020, e-Competitions December 2020, Art. N° 99246* ; ***Laura Lehoczky-Deckers****, The German Government prohibits the acquisition of a telecommunications company by a Chinese industrial group on the basis of the foreign trade and payments ordinance (IMST / Addsino), 2 December 2020, e-Competitions December 2020, Art. N° 98572.*

[*11*] See ***Rafael Baena, Pablo Velasco,*** *The Spanish Government enacts a foreign direct investments mechanism, 17 November 2020, e-Competitions November 2020, Art. N° 98249* ; ***Casto Gonzalez-Paramo, Alfredo Gómez Álvarez, David Antón,*** *The Spanish Government approves the reform of the legal regime that establishes a screening regime for certain*

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*foreign direct investments, 17 November 2020, e-Competitions November 2020, Art. N° 98051* ; ***Pedro Callol, Manuel Canadas Bouwen, Jorge Manzarbeitia, Enrique Fayos, Laura Moya**, The Spanish Government amends the FDI screening regime and temporarily extends the regime to investments made by EU/EEA investors above-given thresholds, 17 November 2020, e-Competitions November 2020, Art. N° 97937* ; ***Adriana Pérez-Gil, Laura Lehoczky-Deckers, Isabella Omrod-Bufill**, The Spanish Government extends its temporary foreign direct investment screening mechanism, 17 November 2020, e-Competitions November 2020, Art. N° 98222*.

[*12*] See ***Joanna Christoforou, Omar Shah, Savas Manoussakis**, The UK Parliament's Act on foreign direct investment receives royal assent, 29 April 2021, e-Competitions April 2021, Art. N° 101011* ; ***Marc Israel, Kate Kelliher**, The UK Government clarifies the scope of the new national security and investment bill, 2 March 2021, e-Competitions February 2021, Art. N° 99595* ; ***Max Edwards, Jason Hewitt, John Adebiyi, Scott C. Hopkins, Aurora Luoma**, The UK Government provides greater clarity on new national security screening rules to be introduced by the national security and investment bill, 2 March 2021, e-Competitions February 2021, Art. N° 99587* ; ***Michele Davis, Sarah Jensen, Thomas McGrath, Megan Yeates**, The UK Government publishes a consultation response which clarifies the national security regime, 2 March 2021, e-Competitions February 2021, Art. N° 99706* ; ***Veronica Roberts, Ruth Allen**, The UK Government publishes revised sector definitions for mandatory notification under the national security screening regime, 2 March 2021, e-Competitions February 2021, Art. N° 99603*.