FOREIGN DIRECT INVESTMENT REVIEW – RECENT DEVELOPMENTS IN EUROPE

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Foreign Direct Investment Review – Recent Developments in Europe

By Peter Camesasca, Horst Henschen & Martin Juhasz

The article provides an overview of recent developments in foreign direct investment ("FDI") review across Europe. In describing what is meant by FDI review, it outlines that there is no unilateral definition for the concept of FDI, but a common trend towards more rigorous screening and extended mandatory filing requirements. Specific jurisdictional updates follow, concerning amendments to existing FDI regimes in the UK and Germany respectively, alongside recent enforcement practice in those jurisdictions. Newly-introduced FDI regimes in the Czech Republic, Denmark, the Netherlands, and Slovakia are summarized and finally, the authors take an outlook to other policy developments, like the European Commission's Foreign Subsidies Proposal, and explore their implications on M&A transactions.

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I. INTRODUCTION

The European Union ("EU") has traditionally been one of the world's most open economies for foreign direct investments ("FDI"). While it remains an attractive and open destination for investment, public officials continue to voice their concerns about investments into strategic companies and key technologies within the EU. The European Commission ("Commission") has recently presented its EU trade policy reflecting the concept of open strategic autonomy.[2] Therein, the Commission maintains its aim to strengthen multilateralism while emphasizing that the EU will take a more assertive stance in defending its interests and values.[3] The Commission particularly seeks to address what it perceives to be unfair trading practices and finds that the EU "*needs to equip itself with tools to operate in a more hostile international environment if necessary.*"[4]

In that context, the Commission reinstated its call to Member States "*to set up and enforce a fully-fledged FDI screening mechanism to address cases where the acquisition or control of a particular business, infrastructure or technology would create a risk to security or public order in the EU.*"[5] The Commission intends to further strengthen cooperation with national authorities and is even considering "*enhancing the cooperation mechanism established by the FDI Screening Regulation.*"[6] This is all part of a broader trend across Europe and beyond towards closer scrutiny of foreign investments and stricter rules on investment review on the basis of public order and security considerations.[7]

This article seeks to describe what is meant by FDI review and provides an overview of recent developments in Europe. It concludes with an outline of other policy developments and their general implications for investments into Europe.

II. NO UNILATERAL DEFINITION OF FDI BUT A COMMON TREND TOWARDS STRICTER FDI REVIEW

There is no unilateral definition of what may be regarded as a relevant foreign direct investment, and Member States apply their own legal tests and standards when it comes to FDI screening. This is in line with Article 4(2) TEU, as to which national security remains the sole responsibility of each EU Member State.[8] In 2019, the EU adopted a framework for the screening of foreign direct investments into the Union (the "EU Screening Regulation"),[9] which entered into full effect on October 11, 2020.

As regards relevant investments, the EU Screening Regulation refers to "*[…] 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 [target] in order to carry on an economic activity in a Member State.*" This shall include "*investments which enable effective participation in the management or control of a company carrying out an economic activity.*"[10] Recital 9 of the EU Screening Regulation excludes portfolio investments, which the Commission considers as being acquisitions of shares or debt that do not result in a controlling interest of the investor.[11]

Most of the EU Member States have further specified what amounts to a relevant investment and have provided for quantitative invest-

2 Communication from the Commission, "Trade Policy Review - An Open, Sustainable and Assertive Trade Policy," COM(2021) 66 final, February 18, 2021.

3 *Ibid.* p. 4 et seq.

4 *Ibid.* p. 8.

5 *Ibid.* p. 20.

6 *Ibid.* p. 20.

7 See OECD Policy Responses to Coronavirus (COVID-19), Investment screening in times of COVID-19 and beyond, 7.7.2020, available at https://www.oecd.org/coronavirus/policy-responses/investment-screening-in-times-of-covid-19-and-beyond-aa60af47/.

8 See also Article 346(1) lit. b) TFEU with regard to measures for the protection of national security, which relate to arms, munitions and war material.

9 Regulation (EU) 452/2019 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, Official Journal LI 79/1.

10 *Ibid.* Article 2(1).

11 Communication from the Commission, "Guidance to the Member States concerning foreign direct investment and free movement of capital from third countries, and the protection of Europe's strategic assets, ahead of the application of Regulation (EU) 2019/452 (FDI Screening Regulation)," C (2020) 1981 final, 25.3.2020.

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ment thresholds within their FDI regimes. For share acquisitions, these are usually calculated on the basis of equity and/or voting rights.[12] With regard to asset acquisitions, national regimes commonly require the acquisition of a separable business unit, or all essential operating resources of a company.[13] Some countries also cover cases where effective participation in the management or control is acquired.[14] Less common is for national FDI regimes to rely on *de minimis* investment thresholds; where those exist, they include relatively low safe harbors (commonly set at a value worth EUR 1 million).[15]

Each jurisdiction has its own particularities regarding the sectors that attract the focus of FDI screening, especially regarding the target activities that require mandatory FDI filing. The list of sensitive sectors and activities in Article 4(1) of the EU Screening Regulation is not fully harmonized within the EU, and Member States have different interpretations of what amounts to a relevant critical infrastructure or technology.[16] Different definitions also come into play when considering a 'foreign' investor. Investments into particularly sensitive sectors, like defense, are usually subject to screening for EU and non-EU investments alike. Conversely, the FDI Regulation stresses the focus on non-EU/EEA investments in the sectors mentioned in Article 4(1) by referring to 'third countries'. Other countries, such as Poland, broaden the definition to non-EU/EEA or non-OECD investors.

Regardless of national particularities, there is a common trend across Europe and beyond towards more rigorous screening and extended mandatory filing requirements. At the time of writing this article, 18 EU Member States have screening mechanisms in place[17] and the trend of a more thorough FDI screening is followed by other countries around the globe.[18] This development has a tangible impact on global M&A transactions and considerably influences their planning. Most of the FDI regimes contain mandatory filing requirements that are backed with suspensory effect and closing prohibitions. A breach of the latter can often be fined or could ultimately also result in criminal sanctions.[19] National authorities engage in closer cooperation and the increasing exchange of information requires a global FDI strategy for multi-jurisdictional transactions.

III. FDI REVIEW IN EUROPE

Europe has seen significant changes in the FDI landscape, reflected by numerous reinforcements of existing regimes as well as the introduction of new regimes. Some illustrative examples are provided below:

A. UK

Having completed its transition and departure from the EU on December 31, 2020, the UK is working to strike trade deals across the globe from its new international footing. In the National Security and Investment Act (the "NSI Law"), which received Royal Assent on 29 April 2021 and is expected to enter into force later this year, the UK government has begun to define a new approach towards inward investments into the UK. In structural terms, this has involved setting up a new Investment Security Unit within the Department of Business, Energy & Industrial Strategy that will be responsible for receiving and managing notifications under the NSI Law and supporting the Minister for Business who will have decision-making power.[20] Additionally, an Office for Investment has been established with responsibilities to guide investment into the UK and encourage investment for strategic projects. The UK government has also announced domestic initiatives such as the Advanced Research and Innovation Agency as a potential support to developers of critical technology.

12 E.g. Germany, Italy, Hungary, Spain.

13 E.g. Germany, France.

14 E.g. Germany, France.

15 E.g. Spain, Italy, Hungary.

16 P. Camesasca, H. Henschen & M. Juhasz, Foreign direct investment screening in Europe: A comparative perspective on differences and commonalities within Europe, *Concurrences* N° 4-2020 pp. 268-272.

17 A list of screening mechanisms notified by Member States to the European Commission is available at https://trade.ec.europa.eu/doclib/docs/2019/june/tradoc_157946.pdf.

18 Countries that have recently tightened their regimes include for example Australia, the U.S., India, and Canada.

19 For example in Austria, France, Germany and Poland.

20 T. Reilly & K. Kingsbury, UK National Security & Investment Law is Approved by Parliament, *Covington Competition*, May 4, 2021, available on Covington Competition at https://www.covcompetition.com/2021/05/uk-national-security-investment-law-is-approved-by-parliament/.

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The NSI Law will have a retroactive effect, applying to any transaction completed after November 12, 2020. Once in effect, mandatory notification obligations will be introduced by the NSI Law for transactions in 17 sensitive sectors where a 25 percent interest in capital and/or voting rights is acquired. Furthermore, the Government will retain broad discretion to 'call-in' transactions occurring in any sector for review if "material influence"[21] is acquired and including asset transactions, if it has reasonable concerns on national security.

These call-in powers endure for up to five years from the date of the transaction, and potentially extend insofar as to allowing scrutiny of transactions occurring outside the UK if the transaction may have implications for supplies or other activities into the UK. A voluntary notification regime will therefore be available, providing a route for investors, who seek legal certainty in relation to transactions that may be covered by the "call-in" powers.

In the meantime and until the NSI Law takes effect, the UK government has been investigating transactions using the pre-existing public interest intervention regime established under the Enterprise Act 2002. This prior regime relies upon the UK's Competition and Markets Authority ("CMA") to provide operational support to Ministers in the review of transactions on a range of public policy grounds, including national security. Specifically, on April 19, 2021, the Secretary of State for the Department for Culture Media & Sport issued a public interest intervention notice in respect of the proposed acquisition of the UK semi-conductor company ARM Limited by US company Nvidia Corporation.[22] The CMA is now due to prepare a report on the USD 40 billion transaction which will inform any further decisions made by the Minister. While waiting for the deal to be cleared, Nvidia has made commitments to maintain ARM's neutrality, an element also considered important when the UK permitted SoftBank's takeover of the company in 2016. Developments on the case may offer an insight into the UK's new approach to FDI, in particular whether the UK's FDI screening tools will be used solely to address national security concerns or wider economic issues as well.

For its part, the CMA has also appeared more proactive in referring transactions to UK Ministers for potential national security or other public policy concerns. On March 3, 2021, the CMA notified the Secretary of State for Business, Energy and Industrial Strategy of potential public interest considerations arising from the proposal by Imprivata, Inc. to acquire Isosec Limited, a developer of software identity tools including for the UK National Health Service. Further, on May 12, 2021, the CMA notified the proposed acquisition of Xilinx by Advanced Micro Devices to the Culture Secretary, likely due to the relevance of Xilinx to UK data infrastructure networks. It remains to be seen (at the time of writing) whether Ministers will take forward a public interest intervention in respect of the Xilinx/AMD transaction; in the meantime, the proposed acquisition of Isosec was abandoned after a Phase II merger control investigation was initiated.

B. Germany

On April 27, 2021, the German government adopted the 17th amendment ("Amendment") to the Foreign Trade and Payments Ordinance ("AWV"), further aligning the German FDI regime with the EU Screening Regulation. The Amendment significantly extended the number of sectors and target activities that require mandatory notification in Germany and also brought significant procedural changes and clarifications.[23] The revised Ordinance entered into force on May 1, 2021 and will apply to all transactions signed thereafter.

The Amendment followed a series of prior legislative changes. In light of the COVID-19 pandemic, the German government had previously adopted the 15th AWV-Amendment in June 2020, which introduced far-reaching filing obligations in the healthcare sector. Subsequently, the first amendment of the Foreign Trade and Payments Act introduced standstill obligations backed by fines and criminal charges in July 2020 for all transactions that require mandatory FDI filing. Together with the 16th AWV-Amendment in October 2020, the German FDI regime was aligned with the requirements of the EU Screening Regulation and the EU cooperation mechanism.[24]

Under the now current regime, mandatory notifications with suspensory effect are required for foreign acquisitions of domestic companies with activities that either fall into the list of defense-related activities (the so-called sector-specific examination), or that concern other sensitive activities under the so-called cross-sectoral examination, such as the operation of critical infrastructures or activities relating to critical technol-

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21 'Material influence' may have expansive meaning if recent UK competition law precedents are applied, and could bring investments of much less than 25 percent in scope of the regime.

22 *Ibid.*

23 For further information see P. Camesasca, H. Henschen & M. Juhasz, Technology Sector under Closer Scrutiny – German Government Significantly Extends the Scope of Foreign Direct Investment Review in Germany, *Covington Competition*, May 6, 2020 available on Covington Competition at https://www.covcompetition.com/2021/05/technology-sector-under-closer-scrutiny-german-government-significantly-extends-the-scope-of-foreign-direct-investment-review-in-germany/.

24 *Ibid.*

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ogies.[25] The Amendment substantially extended the list of sensitive sectors under both the sector-specific and the cross-sectoral examination, and went beyond the list of activities contained in Article 4(1) of the EU Screening Regulation. More specifically, the Amendment also addressed activities that relate to autonomous vehicles or unmanned drones, optoelectronics, additive manufacturing processes (3D printing) and certain network technologies.

25 Those critical technologies *inter alia* include satellite systems, artificial intelligence, autonomous driving and unmanned flying, industrial robots, semiconductors and optoelectronics, IT-security equipment, aerospace goods or technologies, nuclear technology, and quantum technologies.

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Even though the list of sensitive sectors requiring mandatory filing has been significantly extended over the past few years, prohibition decisions are still rare in German FDI control. While decisions of the German FDI regulator are not published, the few interventions became known to the public:

- In July 2018, the German government decided to prevent the acquisition of a minority stake in the power grid operator 50Hertz by a Chinese investor through an investment by the state-owned development bank KfW in the target, as the then pertinent FDI regime did not provide for powers to block the transaction;
- In August 2018, the Chinese undertaking Yantai Taihai Corporation withdrew from the planned acquisition of the German industrial tool maker Leifeld Metal Spinning, after the German FDI regulator threatened to block the transaction;
- In July 2020, the German government blocked a Chinese investor's proposed acquisition of PPM Pure Metals GmbH, a manufacturer of metals used in semiconductors and infrared detectors, including for military applications;
- In December 2020, the German FDI regulator issued a prohibition decision to the Chinese acquirer Addsino Co Ltd, Beijing regarding the acquisition of IMST GmbH, a German-based manufacturer of components with military applications in satellite/radar communications and 5G;[26]
- Besides that, the German KfW acquired a minority stake in CureVac, a biopharmaceutical company inter alia active in the development of COVID-19 vaccines, in order to avoid its potential acquisition by foreign investors;
- Currently, the BMWi is conducting in-depth investigations regarding several investments in the semiconductor industry and also appears interested in the Nvidia/Arm transaction outlined above, with regard to which German state officials referred to a potential impact of the transaction on European digital sovereignty and cybersecurity.

Other jurisdictions

Several other Member States have amended or introduced FDI regimes recently, a trend accelerated by the effects of the COVID-19 pandemic.[27] Some of these Member States include:

a. Czech Republic: On May 1, 2021, a new Czech foreign investment control regime has become applicable through the Act on Screening of Foreign Investments ("FIR Act"). The regime applies to acquisitions by non-EU investors of at least 10 percent share interests in domestic companies involved in sensitive activities such as critical infrastructure including information infrastructure, military equipment and dual-use goods. Relevant transactions will be subject to mandatory notifications with suspensory effect. Other transactions can be reviewed ex officio on national security grounds up to five years after completion of the investment. The Czech Republic also offers voluntary consultations to seek legal certainty.[28]

b. Denmark: The Danish parliament recently passed a new screening mechanism entering into force on July 1, 2021, which is applicable to all transactions that are not completed until September 1, 2021. The bill provides for ex officio investigation powers and introduces mandatory filing obligations for investments into targets active in sectors such as defense, IT security, dual-use goods, critical technology and critical infrastructures. The bill further introduces a voluntary notification process for investments potentially threatening national security and public order. The Danish Business Authority is expected to issue executive orders to provide guidance on the bill in the near future. The introduction of the bill is reported to be partly due to a bid by Chinese company Huawei to build Denmark's 5G network.[29]

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26 P. Camesasca, H. Henschen & M. Juhasz, Foreign Direct Investment – German Government Prohibits Acquisition By A Chinese Buyer, *Covington Competition*, Deember 12, 2020 available on Covington Competition at https://www.covcompetition.com/2020/12/foreign-direct-investment-german-government-prohibits-acquisition-by-a-chinese-buyer/.

27 OECD (footnote 7).

28 See Ministry of Industry and Trade of the Czech Republic on Investment Screening, available at https://www.mpo.cz/en/foreign-trade/investment-screening/.

29 Denmark passes law to screen foreign investments for security risks, May 5, 2020, available on Reuters at https://www.reuters.com/article/denmark-security-investment-idUSL1N2MS1CO.

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c. Netherlands: A Dutch FDI screening mechanism implementing the EU Screening Regulation came into force in December 2020 (the "Implementing Act").[30] The Implementing Act designated the competent contact point in the Netherlands for the EU cooperation mechanism and specified which ministers are responsible for decisions taken under the EU cooperation mechanism. The Implementing Act further defined the sources that may be used for information gathering under the regulation.

   The Dutch government has presented another draft bill, which is currently undergoing legislative procedure. The draft bill contains mandatory notification requirements for investments in sectors such as sensitive technology and supplies of vital processes. The draft bill is currently being amended by the Minister of Economic Affairs and Climate, who has extended its review period.[31] Notably, the bill is likely to have retroactive effect extending back to 2 June 2020.

d. Slovakia: Slovakia's new regime for FDI screening entered into force on 1 March 2021. The regime introduced mandatory notification requirements for acquisitions of control or ownership (exceeding 10 percent of capital or voting rights) in companies operating critical infrastructures, such as transportation; postal services; energy; communication via electronic means; the management of water; finance; information and communication technologies; healthcare and pharmaceuticals; or heavy industry and agriculture.

IV. OTHER POLICY DEVELOPMENTS AND THEIR GENERAL IMPLICATIONS

The latest developments in FDI screening and their underlying trade policy considerations are echoed by other legislative proposals, which will further impact foreign investments into the EU. While foreign investments are still acknowledged as a welcome source of employment, growth and competitiveness, the regulatory hurdles that arise continue to increase.

Not long ago, the Commission published its proposal for the regulation of foreign subsidies (the "Foreign Subsidies Proposal") and therein *inter alia* suggests a pre-closing notification requirement for transactions that may have benefitted from financial contributions of non-EU countries.[32] The proposal is a result of the Commission's public consultation that followed its White Paper on foreign subsidies from last year.[33] More specifically, the proposal suggests a mandatory notification requirement for acquisitions of EU targets, where the EU turnover of the company to be acquired (or of at least one of the merging parties) is equal to or higher than EUR 500 million and where the undertakings concerned received a foreign financial contribution of at least EUR 50 million within the last three years.[34] Companies based outside the EU that receive foreign state support in any form will therefore need to consider the implications of the proposed regime and potential filing requirements for their future EU-bound activities.

Already by now, the long-established merger control assessment is accompanied by a multi-jurisdictional analysis of FDI-related risks in global transactions. The Foreign Subsidies Proposal may add another pre-closing filing requirement for certain transactions and therefore brings additional regulatory complexity for investments into Europe. Even though the majority of investments into Europe that are subject to mandatory filings, regardless of whether under the current merger control or FDI laws, receive clearance by the competent authorities, the increased scope of mandatory filing requirements and the substantial information required to conduct a filing assessment have a tangible impact on investment planning. Lengthy review periods (often exceeding statutory review periods), uncertainty as to final outcomes and substantial amounts of information requested by screening authorities are detrimental to Europe's attractiveness for foreign investments. Business associations have already complained that the broad scope of mandatory FDI filing requirements could force small and medium-sized manufacturers to withdraw from activities in sensitive sectors.[35] The right balance between the legitimate purposes of investment screening and an undistorted flow of investments will therefore need to be further explored.

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30 Ministry of Economic Affairs and Climate, Wet, Staatsblad 2020, 491 of 3.12.2020, available at https://zoek.officielebekendmakingen.nl/stb-2020-491.html.

31 Minister of Economic Affairs and Climate, Investment review planning system to minimise risks to national security, Government Letter, December 8, 2020, available at https://www.tweedekamer.nl/kamerstukken/brieven_regering/detail?id=2020Z24227&did=2020D50922.

32 The Commission Proposal for a Regulation Of The European Parliament And Of The Council on foreign subsidies distorting the internal market, COM(2021) 223 final, May 5, 2021.

33 European Commission, White Paper on levelling the playing field as regards foreign subsidies, COM(2020) 253 final, June 17,.2020.

34 Foreign Subsidies Proposal (footnote 32), Article 18.

35 As stated in a letter from the German Mechanical Engineering Industry Association (VDMA) to the German Ministry of Defense.

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