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Foreign Investment Review in Europe: Key Considerations for Investors and Latest Developments Prompted by COVID-19

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Introduction

Global foreign direct investment (FDI) amounted to 1,426 billion USD in 2019[1]. In recent years, a number of countries around the world have implemented measures to strengthen their FDI review mechanisms. Undoubtedly, this worldwide trend is having an impact on international mergers and acquisitions transactions as illustrated by a number of cases highlighted in the media.

Recently, there have been a number of important legal developments at European and international levels, including the broadening and enhancement of existing foreign investment review mechanisms in the United Kingdom, France, Germany, Italy and the United States, to name but a few.

Over the last several months, this trend has increased as a result of the COVID-19 pandemic and a number of European countries have accordingly strengthened, or are in the process of strengthening, their FDI regulations.

In parallel with these national initiatives, the European Union's new Regulation on FDI came into force on April 10, 2020, providing the European Commission (the "Commission") with a mechanism to influence FDI reviews, but leaving ultimate decision-making powers at the Member State level.

In response to the COVID-19 pandemic, the Commission is paving the way for EU Member States to tighten their foreign investment rules through a blend of policy measures and an exercise of its role under the Regulation. On March 25, 2020, the Commission issued a Guidance Paper[2] addressing potential takeovers by non-EU investors of European companies and assets in "strategic industries" during the pandemic. The Commission has prompted Member States to launch FDI screenings, capital controls, and other options to shield European businesses, infrastructure, or technologies of strategic importance from foreign takeovers. It also strongly encourages all Member States that do not have screening mechanisms to establish these as quickly as possible.

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[1] OECD, "FDI in figures – Global FDI increased in 2019 but was still struggling when Covid-19 hit," April 2020.

[2] 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), March 25, 2020.

With the emergence of a number of common trends, including:

- the expansion of the scope of screenings to include new fields relating to economic and technological security,
- longer review periods by national authorities,
- the lowering of thresholds triggering the screening of foreign investments, and
- the hardening of applicable sanctions,

and due to the potential impact of such trends in the timetable and completion of cross-border mergers and acquisitions transactions, it is important for foreign investors to understand the existing regulations and reforms in relation to FDI in certain key European jurisdictions, such as: the United Kingdom, France, Germany, Italy and Spain.

Additionally, given the enhanced focus on establishing fully-fledged screening regimes in all Member States and the broader economic impacts of the COVID-19 pandemic, foreign investors can expect greater rigor in assessing transactions across the region.

This paper will also briefly discuss certain CFIUS[3] implications relating to acquisitions of European companies by foreign investors.

United Kingdom

No restriction on foreign investment per se in the U.K., but the Government has limited legal powers for intervention, on national security or certain other public interest grounds, and has proposed an extension of these powers.

I. U.K. foreign investment regime mainly draws upon the domestic competition regime whereby certain mergers (whether wholly domestic or with a foreign acquirer) may be reviewed and authorized, as the case may be, by the U.K. competition authority (the CMA):
    - on "public interest grounds" provided that the U.K. target has an annual turnover of more than £70 million or the merger creates a combined share of supply of 25% or more or increases an existing share of supply that is 25% or more and that the merger may impact national security, financial stability or media plurality or standards;
    - on "special public interest grounds," when, irrespective of any merger threshold, they concern the development/production of military or dual-use items, certain computing hardware technologies and quantum technologies (the "sensitive sectors"), or media companies with a 25% or more share of their relevant media (e.g., newspapers or broadcasting); or
    - if the U.K. target has an annual turnover of £1 million and a share of supply that is already at 25% and involves the development/production of military or military/civilian items, certain computing hardware technologies and quantum technologies.

II. U.K. merger review is based on a voluntary notification, with no mandatory pre-clearance filings, although the CMA can "call in" mergers for review or be directed to do so by the Government. The review involves a two-stage investigation process:
    - a "Phase 1 investigation" (approx. 40 working days) to determine if competition issues are raised; and

[3] Committee on Foreign Investment in the United States.

- a “Phase 2 investigation” (approx. 24 weeks) to analyze the competition or public interest concerns and make a conclusion as to how they should be addressed or if the merger should be blocked.
- For a public interest grounds review, a Phase 2 report is issued by the CMA to the Government which decides on the ruling to make and relevant remedies (including blocking the merger). Judicial review of Government rulings is possible.

III. The Industry Act 1975 grants further powers (not exercised so far) to the Government to block foreign takeovers of “important manufacturing undertakings” where there is a direct or indirect change in control to a “non-U.K. person,” and the Government determines that the “manufacturing industry undertaking” is of “special importance” to the U.K. or any substantial part of it.

IV. Additional constraints on foreign takeovers include the golden shares regime[4] and the requirement for Ministry of Defence contractors to notify the Ministry of any planned change of control.

V. The Government encourages informal notification of mergers that may involve businesses in the “public interest” sectors so that, where appropriate, a preliminary view may be given on the “national security” issue.

VI. Proposed Reform – Following the Government’s October 2017 “National Security and Infrastructure Investment Review” (which has already led to the introduction of the “sensitive sectors” referred to above), in July 2018 the Government announced further proposals for national security review of transactions, still on a “voluntary notification” basis but with the Government having the right to call in for review mergers that have not been voluntarily notified, where the “merger” or acquisition involves the acquisition of:

- more than 25% of an entity’s shares or votes;
- significant influence or control over an entity; or
- further acquisitions of significant influence or control over an entity beyond the above thresholds.

VII. A key part of the proposals is a detailed statement of policy intent (which the Government has issued in draft) that will set out when and how the Government expects national security risks to arise from the above trigger events, by looking at “target risks” (i.e. entities or assets the acquisition of control of which could be used to undermine national security, and the sectors of the economy where the Government expects these risks are more likely to arise), “trigger event risks” (i.e. the nature of the control or influence over the target assets that is being acquired) and “acquirer risks” (i.e. whether the acquirer is a party which the Government considers is more likely to pose a national security risk through the acquisition and whether a foreign state may be of concern because of the influence or control it can have over relevant U.K. assets through its law/regulatory-making control of investors in those assets who are based in the relevant foreign state). The Government is currently reviewing feedback received on these proposals.

VIII. In December 2019, the National Security and Investment Bill was announced in the Queen’s speech. Its purpose is to strengthen the Government’s powers to scrutinize and intervene in transactions to protect national security. The three main elements of the proposed legislation are: a notification system allowing businesses to flag transactions with potential security concerns to the government for quick, efficient screening; powers to mitigate risks to national security—by adding conditions to a transaction or blocking as a last resort, plus sanctions for non-compliance with the regime; and a safeguarding mechanism for parties to appeal where necessary. The bill awaits its second reading.

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[4] The U.K. government currently holds golden shares in few companies (e.g. BAE Systems).

France

No restriction on foreign investment per se in France, whether non-EU or EU investments, but prior authorization from the Ministry of Economy required when investment is made in identified sensitive sectors.[5]
In the context of the COVID-19 pandemic, the French Ministry of Economy decided to modify its FDI regime on April 29, 2020 and announced that the 25% voting right threshold relating to non-EU and non-EEA investments mentioned below under point 1 will shortly be lowered to 10% with respect to investments in listed companies until December 31, 2020. In addition, biotechnology has been included in the list of sensitive sectors mentioned below under point 4 by Ministerial Order of April 27, 2020.

I. Foreign investment in a French law governed entity encompasses (a) the direct or indirect acquisition of a controlling stake; (b) the acquisition of all or part of a line of business; (c) for non-EU or non-EEA investors only, the acquisition of more than 25% of the voting rights.

II. Are considered as foreign investors, (a) any foreign individual, (ii) any French individual with foreign tax residence, (c) any foreign entity or (d) any French entity controlled by any of the aforementioned individuals or entities. In addition, any person or entity that is part of a foreign investor's chain of control would also qualify as a foreign investor for the purposes of the French foreign investment regulation.

III. Prior authorization from the Ministry of Economy is required for foreign investments in sensitive sectors affecting the exercise of public authority, public order, public safety and national defense.

IV. Identified sensitive sectors include, among others, the gambling industry (with the exception of casinos), private security services, businesses involved in the research and development or manufacture of pathogens or toxic substances, wiretapping, electronic data and mail interception, services relating to the security of information technology systems and products, cryptology, energy and water supply, spatial operations, electronic communications networks and services, protection of public health, cybersecurity, artificial intelligence, robotics, additive manufacturing, semi-conductors, big data storage, political and general press, agricultural activities involving food security objectives and biotechnology.

V. In case of doubt as to whether the proposed investment is subject to review, target or foreign investor (acting in agreement with the target) may, assuming there is a concrete investment proposal, request an opinion from the Ministry of Economy. Such opinion shall be issued within two months.

VI. Procedure to be followed for prior authorization of foreign investment in sensitive sectors:
   - filing of an application for authorization once the contemplated investment is "sufficiently advanced" (could be prior to the signing of definitive agreements if a document attesting that the transaction has reached a sufficiently advanced stage is available, as such document must be provided with the application);
   - Phase I review (mandatory): 30-business day period[6] whereby the Ministry of Economy is required to assess whether the contemplated investment (i) does not require prior authorization, (ii) is unconditionally authorized, or (iii) requires Phase II review in order to determine whether sensitive national interests may be protected by imposing specific conditions.

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[5] On December 31, 2019, the French government reshaped the French foreign direct investment rules and strengthened the review process of the foreign investments in sensitive sectors, the new regime of which is outlined therein.

[6] The timeframe does not start until the application file is deemed complete by the Ministry of Economy, so it is highly recommended to ask for confirmation on completeness of the file to ensure that the 30-business day period has started.

- Phase II review (if required by the Ministry of Economy): additional 45-business day period whereby the Ministry of Economy must determine whether the authorization request is (i) rejected, (ii) granted or (iii) granted under specific conditions.
- If no answer is provided at the end of the Phase I or Phase II periods, the authorization is deemed denied.

VII. Conditions with which foreign investors may be required to comply are mainly centered on:

- guaranteeing the sustainability and security of the sensitive activities carried out by the target,
- guaranteeing the protection of the target's know-how and preventing access thereto,
- adapting the target's internal management and organization as well as the rights of the investor over the target, and
- determining the information to be provided to public authorities.

In particular, the Ministry of Economy may condition the authorization on the transfer by the investor to an approved third-party of (i) a stake or (ii) sensitive assets of the target.

Such conditions may be revisited at the investor's request or at the Ministry of Economy's initiative if specific circumstances arise.

VIII. In case of non-compliance, several enforcement measures may be taken by the Ministry of Economy, who may ultimately order the winding up of the investment. Other measures may include the suspension of voting rights or dividend distributions, restriction on the investor's rights to dispose of the sensitive assets, appointment of a trustee entitled to challenge the decisions of the target's management. The Ministry may also order daily penalty payments of up to EUR 50,000 in case of persisting breach. Failure to comply may also result in criminal penalties (imprisonment up to 10 years and a fine of up to twice the amount of the transaction which can be multiplied by five for legal entities).

IX. In the past, the French government has rarely used its powers to forbid FDI in France and, in sensitive cases, the government usually imposes conditions on foreign investors.

Germany

No restriction on foreign investment per se in Germany, but the Federal Ministry for Economic Affairs and Energy (the "Ministry") may review foreign investments and prohibit or restrict them if they pose a threat to public order or security.

I. Foreign investment encompasses the direct or indirect acquisition by a non-EU/EFTA investor of (a) at least ten percent of the voting rights in a German company engaged in critical infrastructure or other defined sensitive areas (see below) or (b) at least 25 percent of the voting rights in a German company active in other sectors.[7]

II. Critical infrastructures include, among others, energy, water (public), nutrition, information technology, telecommunication, health, finance and insurance and transportation. Other defined sensitive areas include customized software supporting operators of critical infrastructures, monitoring of telecommunication, cloud computing services, telematics infrastructure in the German health system, and media of certain relevance.

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[7] The calculation of the voting rights includes the voting rights of third parties in the domestic company (i) in which the acquirer holds at least 10/25 percent of the voting rights, or (ii) with which the acquirer has concluded an agreement on the joint exercise of voting rights.

III. A formal investigation can be commenced by the Ministry within three months after it has obtained knowledge of the transaction.

IV. Generally, there is no notification requirement for deals involving foreign investors, provided that investments in critical infrastructure or other defined sensitive areas (see above) need to be notified to the Ministry.

V. The Ministry can prohibit or restrict a foreign investment if such investment is found to pose an actual danger to public order or security requiring an approval by the federal government. This can include the imposition of certain conditions or instructions upon the investor to ensure public order and security such as:

- orders to continue related production segments,
- location guarantees, or
- obligations not to transfer certain production segments to foreign countries.

VI. It has become a matter of best practice even in cases where there is no notification requirement that the investor applies in advance for a certificate of non-objection to clear the issue and allow for closing of the transaction. The procedure to be followed in this case is as follows:

- Filing of an application with the Ministry.[8]
- Ministry to issue a certificate of non-objection if there is no threat to public order and security.
- The certificate of non-objection is deemed to have been issued if no review procedure is opened by the Ministry within two months of receipt of the application.
- If an in-depth review procedure is commenced, the Ministry has four months to decide whether to prohibit or restrict the transaction.

VII. Specific rules apply for acquisitions by foreign (including EU/EFTA) investors of companies operating in sensitive security areas (i.e. manufacturing of military equipment and products with security IT features used in classified government data processing) and high-grade earth remote sensing systems.

VIII. Investments in areas other than sensitive security areas, including investments in critical infrastructure or other defined sensitive areas (see above), can be closed without an approval by the Ministry or the issuance of a non-objection certificate but have to be unwound if the Ministry concludes that there is a threat to public order or security in accordance with the principles laid out above. Typically, the transaction documents contain corresponding closing conditions to avoid such a situation and the transaction is only closed after the situation has been cleared.

IX. The German government recently presented a proposal for changes to the foreign investment rules, part of which implement the EU Screening Regulation (the "Regulation"). The amendments to the Foreign Investment Act proposed by the government are currently being discussed in parliament. In addition, there will be amendments to the Foreign Investment Regulation to be adopted by the government.

In addition to the implementation of a mechanism for cooperation with other Member States and the European Commission, further key changes deriving from the Regulation are:

- Prohibition or restriction of foreign investment in areas other than sensitive security areas (for which, as mentioned, specific rules apply) will no longer require that such investment is found to pose an actual danger

[8] Such application shall cite the acquisition, the acquirer, the domestic company to be acquired and the basic features of the respective fields of business of acquirer and domestic target.

to public order or security. It will be sufficient that such foreign investment is found to be likely to affect public order or security. This change lowers the required degree of endangerment and implies a more forward looking perspective, which includes a foreseeable potential threat to or adverse effect on the public order or security in the future as a result of foreign investment.

- The list of defined sensitive areas (see above) will be expanded, to a significant extent also in light of the COVID-19 pandemic, to include (i) services required to ensure undisturbed operation of public communication infrastructures of public authorities and organizations with security functions, (ii) manufacturing and development of certain key health care products—including for example drugs that are essential for public health care like vaccines or antibiotics as well as their active ingredients, medical personal protective equipment, medical products like ventilators for treatment of life-threatening and highly contagious infectious diseases, and diagnostic tests for proof of an infectious agent—and of related components/pre-products, manufacturing facilities and manufacturing/development technologies, (iii) mining and processing of critical raw materials or their ores and (iv) certain key technologies, such as artificial intelligence, robotics, semiconductors, biotechnologies and quantum technologies.
- The particular foreign investor and its background will be taken into account in determining whether a foreign investment is likely to affect public order or security. For example, it will be taken into account whether the foreign investor is directly or indirectly controlled by the government, including other state bodies or armed forces, of a third country, including through ownership structure or through funding, which exceeds an immaterial level. Funding may, for example, not exceed an immaterial level where a foreign state controlled bank merely grants the investor an overdraft credit on its business account, which is market standard in terms of interest rate and volume.

Key changes not deriving from the Regulation include:

- Closing of investments in critical infrastructure or other defined sensitive areas without an approval by the Ministry or the issuance of a non-objection certificate will be legally void and will become valid retroactively upon approval or issuance of a non-objection certificate.
- In addition, in such cases certain actions will be prohibited prior to approval or issuance of a non-objection certificate in order to make sure that the purpose of the foreign investment control is not undermined. For example, it will be prohibited to enable the foreign investor to exercise voting rights or to grant the investor access to information relating to critical technology pending the approval procedure.

X. The proposed changes will become effective—possibly with some changes—shortly. The process will be accelerated by concerns regarding the sell-out of weakened German businesses to Chinese or other non-EU buyers as a result of the COVID-19 pandemic. The Federal Minister for Economic Affairs said in parliament that German businesses will be protected against "becoming victims of takeover attempts only because share prices are somewhat lower at the moment than at other times."

Italy

Prior notice to, and authorization from, the Italian Government is required in relation to investments made in identified sensitive strategic sectors. In the context of the COVID-19 pandemic, on April 8, 2020, Italy with the issuance of Law Decree No. 23/2020 (the "Covid Decree"), expanded its FDI regime to a number of additional sectors and introduced a stricter temporary regime applicable until December 31, 2020 requiring notification also in the case of acquisitions by EU persons.

I. The Italian FDI regime requires notification to the Italian Government of transactions in the defense, transportation, energy and communications sectors.

II. Under the new provisions approved in the context of the COVID-19 pandemic, an authorization is now required in relation to transactions in all sectors provided for in the EU Regulation on FDI Screening (i.e., sectors listed in Article 4(1)(a-e) of Regulation (EU) 2019/452), including among others (i) critical infrastructure including energy, transport, water, health, supply, communications, media, data processing or storage, aerospace, including sensitive facilities, and (ii) supply of critical inputs, including energy or raw materials, as well as food security. The Italian Government reserved the authority to issue implementing regulations to better identify the specific activities or assets to be considered strategic or critical.

III. The notification requirements apply as follows:

Defense and National Security

- any person (regardless of nationality) acquiring an interest in a strategic entity in the sector of defense and national security exceeding the thresholds of 3%, or otherwise increasing the purchaser's holding to exceed the 5%, 10%, 15%, 20% or 25% thresholds; and

Other Sectors

- non-EU persons acquiring a controlling interest in a strategic entity in the sector of (a) energy, transportation and communications *and* (b) *from April 2020*, in all sectors provided for in the EU Regulation on FDI Screening (including, among others (i) critical infrastructure including energy, transport, water, health, supply, communications, media, data processing or storage, aerospace, including sensitive facilities, and (ii) supply of critical inputs, including energy or raw materials, as well as food security);

- In response to the COVID-19 pandemic, a stricter temporary regime applies until December 31, 2020. In particular, a notification is also required in the case of (i) acquisitions by a non-EU person of interests exceeding 10% (and a value of Euro 1 million), 15%, 20%, 25% or 50%; or (ii) acquisitions by any EU person acquiring a controlling interest.

IV. Companies active in the strategic sectors must also notify the Italian Government of certain key corporate transactions (e.g., mergers, de-mergers, winding-up, transfer of business, transactions that may result in a change of ownership or control of a strategic asset, etc.).

V. In case an asset or company falls within the scope of the Italian FDI regime, the following procedure applies:

- filing of a request for authorization with the office of the Italian Prime Minister prior to the closing/implementation of the relevant transaction[9];

- a 45 business day review period which may be suspended once for a period up to 20 days if a request of additional information is made by the Government;

- the approval is deemed granted if no measure is issued within the applicable review period.

VI. Prior authorization may be granted subject to certain undertakings or conditions relating to:

- the continuity of supply,

[9] The relevant provisions refer to a term of 10 days after the completion of the acquisition. In practice, it is advisable to file the notification upon signing of the transaction.

- the protection of IP and manufacturing in Italy of specific products used in military end-markets, assurances on job security, and
- other similar conditions.

VII. Additional conditions may relate to (i) ongoing monitoring requirements to ensure compliance with conditions imposed, (ii) safety measures, and (iii) organizational and structural measures aimed at ensuring confidentiality of information and technological know-how of the target.

VIII. Failure to comply may result in the suspension of voting rights and the requirement to sell the relevant shares (in case of a veto of the transaction) and monetary sanctions with a fine of up to twice the value of the transaction, and in any event at least 1% of the combined turnover of the companies involved in the transaction. Depending on the circumstances, criminal sanctions may also apply.

IX. Regardless of whether an actual risk or threat to national interests exists, the acquisition by a non-EU person of an entity holding a strategic asset may be authorized only to the extent that reciprocity applies between Italy and the country of origin of the investor.

X. The Italian Government's powers can only be exercised in the event the transaction may give rise to:
- a threat of serious damage to the essential interests of national defense and security (with respect to strategic assets in these sectors), or
- a threat to national safety and public order, including continuity of operations and supply (with respect to strategic assets in the energy, transportation or communication sectors identified in the Covid Decree by reference to those listed in the EU Regulation on FDI Screening).

XI. In the past the Italian Government has made limited use of the above powers. Based on the latest publicly available survey on Italian FDI controls, between 2013 and 2018 only one acquisition was vetoed by the Italian Government on the grounds of national security. In a limited number of cases, the Italian Government decided to impose conditions to the relevant transaction[10].

Spain*

Due to the COVID-19 pandemic, a new regime on foreign investment in Spain was established on March 18, 2020 (new article 7bis of the 19/2003 Spanish Foreign Investment Law introduced by Royal Law Decrees 8/2020 and 11/2020), which requires prior government authorization when a foreign investment is made in a number of Strategic Sectors or by a Specifically Restricted Investor.

I. Direct foreign investments in Spain are deemed to be (i) those investments as a consequence of which the foreign investor acquires a participation of or above 10% of the share capital of the Spanish company; or (ii) a corporate transaction, act or legal procedure as a consequence of which the foreign investor effectively participates in the management or control of a Spanish company provided that the foreign investment is carried out by non EU-EFTA residents or by residents in the EU-EFTA whose beneficial owner is resident in a country outside the EU-EFTA. The existence of relevant beneficial ownership shall be understood to occur when the beneficial owners ultimately hold or control, directly or indirectly, 25% or more of the share capital or the voting rights of the investor or when, by other means, they exert direct or indirect control over the investor.

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[10] The largest fines imposed so far by the Italian Government include the €74.3 million fine for alleged lack of notification in connection with the attempted 2017 takeover by Vivendi of TIM. TIM appealed such decision before the administrative courts and the relevant proceeding is currently pending.

II. Strategic Sectors include:
   - Critical infrastructures, both tangible and virtual (including infrastructures in energy, transport, water, healthcare, communications, media, data storage and processing, aerospace, defense, finance or sensitive installations) as set forth in the Law 8/2011 establishing measures to protect the critical infrastructures.
   - Critical technologies and dual-use items (including A.I., robotics, semiconductors and cybersecurity, aerospace, defense, energy storage, quantum and nuclear technologies, nanotechnology and biotechnology) as defined in article 2, section 1 of Regulation (EC) No 428/2009 of 5 May 2009 setting up a Community regime for the control of exports, transfer, brokering and transit of dual-use items.
   - Fundamental supplies including energy (electricity and hydrocarbons) and supplies affecting raw materials or food safety.
   - Sectors with access to sensitive information (including personal data) affecting public order, healthcare or security.
   - Media.

III. Specifically Restricted Investors means any Non EU/EFTA residents falling in any of the following categories:
   - investors directly or indirectly controlled by the government of a third country (including its governmental bodies and armed forces);
   - investors having made investments or participated in businesses related to security, public order or public health (including Strategic Sectors) in other EU member states; or
   - investors in respect of which an administrative or judicial procedure based on criminal or illegal activities has been initiated in any EU member state or in their home state or in any other state in the world.

IV. The governmental authority responsible for authorizing investments is, at this stage, the Cabinet itself. Investments below 1 million euros are exempt. Investments (i) equal to or above 1 million euros but below 5 million euros; or (ii) in respect of which the price was agreed (including by binding offer) prior to March 18, 2020, will be handled and eventually authorized within a 30-day period by the Directorate General of International Trade and Investments (*Dirección General de Comercio Internacional e Inversiones*), which operates within the Ministry of Economy.

V. If the investment cannot benefit from the simplified procedure and therefore must be authorized by the Cabinet, the Cabinet has six months from filing to answer.

VI. Failure to apply for prior authorization may result in monetary penalties with a fine which can be up to the amount of the relevant transaction. As for civil sanctions, any transaction completed in breach of this regime shall be void and will lack any legal effect as long as it has not been authorized.

VII. The new regime lacks clarity and poses numerous interpretative issues, which are expected to be clarified by further regulation.

EU Rules and Policy Measures

The European Union has an FDI screening framework set out in the Regulation on Foreign Direct Investment Screening that came into force on April 10, 2020, and will take effect on October 11, 2020.

Although the Commission does not itself have formal enforcement powers, either to approve or block FDI[11], it can intervene in national-level screening by requesting information from Member States, and exercise influence by issuing an official "opinion" on the grounds of "public order and security." Any deviation from its opinion must be justified by the Member State. Additional details on the EU framework are set out below.

I. Member States may maintain, amend or adopt mechanisms to screen FDIs in their territory on the grounds of security or public order in accordance with the EU-wide framework, as follows:
   - The relevant rules and procedures must be transparent, not discriminate between third countries and provide for a timeframe;
   - There must be procedural rules, to protect confidential information, to appeal against decisions of national authorities, as well as measures to identify and prevent circumvention of the screening mechanisms and screening decisions;
   - The Regulation also sets out a list of factors that may be taken into consideration in determining whether an FDI is likely to affect security or public order, such as the potential effects on: critical infrastructures and technology, supply of critical inputs, access to sensitive information and the freedom and pluralism of the media. Other factors that may be taken into account include, among others, whether the foreign investor is directly or indirectly controlled by the government; and
   - Member States must notify to the Commission their existing screening mechanisms, or any subsequent amendments/newly introduced schemes, within 30 days from, respectively, the entry into force of the Regulation or of the amendment/new scheme.

II. Commission screening on the grounds of security or public order applies to foreign investments, which are likely to affect projects or programs of Union interest[12], and would apply alongside existing EU sectorial legislation. In particular:
   - The Commission may issue an opinion to the Member State in which the foreign investment is planned or completed; and
   - The Member State concerned shall take "utmost account" of the Commission opinion and provide an explanation where the opinion is not followed.

III. A cooperation mechanism between Member States and the Commission allows for an exchange of information on FDIs, following different procedures depending on whether the FDI is undergoing screening or not. In particular:
   - Where the FDI is undergoing screening in one Member State, the latter is required to notify the Commission and other Member States. Member States may submit comments and the Commission may issue a non-binding opinion on the notified transaction within certain deadlines. The Commission must issue a non-binding opinion if at least one third of Member States consider that a FDI is likely to affect their security or public order. The reviewing Member State is obliged to give "due consideration" to the Commission's opinion and to comments from other Member States;

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[11] Foreign investment for the purposes of the Regulation includes a broad range of investments establishing / maintaining lasting direct links between third country investors and undertakings performing an economic activity in Member States, but does not include 'portfolio investments' (previously defined in EU law as share acquisitions with the sole intention of making a financial investment and no intention to influence the management / control of an entity).

[12] Such projects or programs may involve substantial EU funding, or be established under EU law and related to critical infrastructure, technologies or inputs. Selected areas (and related projects) include research (Horizon 2020), space (Galileo), transport, energy and telecommunication networks (Trans-European Networks—TEN).

- Where a Member State considers that a FDI planned or completed in another Member State, which is not undergoing screening in that Member State is likely to affect its security or public order, or has relevant information in relation to that FDI, it may provide comments to that Member State. The Commission may likewise issue an opinion in such cases, if the transaction affects the security or public order of more than one Member State. The Commission *must* issue a non-binding opinion if one third of the Member States consider that an investment likely affects their security or public order. The Member State in which the FDI takes place will give "due consideration" to the comments and the opinion; and
- Notably, the Regulation does not, in the latter case, force a Member State to review a transaction if no FDI control regime exists or the existing regime does not apply where the FDI is taking place. However, as previously mentioned, there is currently a strong push at the Commission and Member State level to establish FDI control regimes in all EU countries. And, at least for this crisis period, governments will likely find additional regulatory means beyond FDI control to restrict or block transactions in industries of concern.

The Commission has emphasized that during the COVID-19 pandemic, Member States may protect European businesses in "strategic industries" or, "strategic infrastructure" from takeovers as these constitute threats linked to a "public health emergency," thereby relevant to the protection of Europe's security and public order.[13] While protection of health and medical research companies are a key focus, relevant sectors to be prioritized for screening also include energy, transport, water, communications, media, data processing or storage, aerospace, defense, electoral or financial infrastructure, sensitive facilities or related land and real estate. Beyond that, the Commission is also specifically concerned with shielding European companies in the tourism sector (airlines, hotels, cruise operators) from foreign investors seeking to "exploit" the crisis.

Presently, the Commission is developing more concrete plans to protect European industries. Beyond FDI review, it has indicated strong support of the following types of measures:

- Portfolio investment screening
- Protection against "predatory buying" and threats to financial stability
- Protection of start-ups/undervalued companies
- Golden shares/nationalization
- Compulsory licenses on patented medicines

CFIUS Approach to Certain EU Investments

Under certain situations, a foreign acquisition of a European company by a non-European company may fall within the jurisdiction of the Committee on Foreign Investment in the United States (CFIUS).

I. Under U.S. law, the U.S. President may review the national security implications of acquisitions of, or investments in, a U.S. business by foreign persons and may block or unwind such transactions when they threaten U.S. national security. The U.S. President has delegated these national security reviews to CFIUS, an inter-agency committee chaired by the U.S. Treasury Department.

II. CFIUS jurisdiction was recently expanded by the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA). CFIUS reviews have traditionally covered only acquisitions or investments that could result in a foreign person acquiring "control" of a U.S. business. CFIUS bases its "control" analysis on whether, as the result of an

[13] Guidance Paper, p. 1.

investment in a U.S. business, a foreign person has the power to make or influence key decisions for that business. Control is not based on the amount of equity being acquired alone, and CFIUS frequently asserts jurisdiction over minority investments based on governance rights or extraordinary veto rights. Such transactions are known as “covered control transactions” under the FIRRMA regulations.

III. FIRRMA, which was enacted in August 2018, extended CFIUS jurisdiction to certain non-controlling foreign investments. Under FIRRMA, CFIUS may assert jurisdiction over non-controlling foreign investments in U.S. businesses engaged in critical infrastructure; certain critical technologies and those that maintain or collect sensitive personal data of U.S. citizens (so-called “TID U.S. businesses” under the FIRRMA regulations). These non-controlling investments are known as “covered investments” under the FIRRMA regulations.

IV. This extension of jurisdiction applies when these investments afford the foreign investor access to certain types of information and certain governance and decision-making rights in a TID U.S. business. Non-controlling investments by certain investors from close U.S. allies, including Great Britain, Canada and Australia, are exempt from CFIUS’s expanded jurisdiction over TID U.S. businesses. Investors from these countries that qualify for the exemption are known as “excepted investors” under the FIRRMA regulations.

V. Prior to enactment of FIRRMA, the CFIUS process was purely voluntary in that transaction parties had the discretion to seek CFIUS clearance for a particular deal. Parties that seek and obtain clearance for a transaction receive the statutory safe harbor from further CFIUS review of the transaction.

VI. FIRRMA changed the regulatory scheme by imposing mandatory filing requirements for two types of transactions. The first is any transaction that results in the acquisition of a direct or indirect voting interest of 25 percent or greater in a TID U.S. Business by an entity in which a foreign government holds a 49 percent or greater voting interest. Substantial interest investments by government-controlled entities from excepted foreign states are exempt from the mandatory filing requirements set forth in the final rules.

VII. The second is any covered control transaction or covered investment by a foreign entity in a TID U.S. business that produces or develops a specified set of “critical technologies” that are designed for use or utilized in one of 27 critical technologies sectors listed in the regulations. These generally include manufacturing activities in the defense and aerospace, semiconductor, petrochemical and biotechnology industries.

VIII. CFIUS may assert jurisdiction over an acquisition of one non-U.S. company by another non-U.S. company when the target has U.S. businesses, such as branch offices or subsidiaries in the United States. In such cases, the reach of CFIUS generally extends only to those U.S. businesses, not to the non-U.S. assets of the acquirer, nor does CFIUS typically assert jurisdiction over mere exports to the United States made to non-related U.S. importers.

IX. CFIUS has on many occasions reviewed transactions involving European companies whose only connection to the United States is a U.S. branch or subsidiary. In 2016, then-President Obama took action to block a Chinese acquisition of the U.S. assets of the German semiconductor company, Aixtron, based on a recommendation by CFIUS.

X. Once CFIUS decides that a transaction is within its jurisdiction, it conducts an analysis of any national security risks posed by the transaction.

- The CFIUS guidance provides that “National Security Risk is a function of the interaction between threat [whether the foreign person has the capability or intent to cause harm] and vulnerability [whether the nature of the U.S. business or some weakness in the system creates a susceptibility to harm], and the potential consequences of that interaction for U.S. national security.”

- CFIUS regularly scrutinizes export control and classified contracts issues as part of this analysis, working closely and in parallel with the U.S. government agencies with jurisdiction over those matters.
- In the Aixtron case, the U.S. Treasury Department said in a statement that the decision was based on the risks posed by "the military applications of the overall technical body of knowledge and experience of Aixtron."

XI. In the past 20 years, the focus of CFIUS has extended considerably beyond its initial focus of acquisitions in the defense sector, to deals involving a range of U.S. industries considered to be "critical infrastructure" or "critical technologies." These include energy, telecommunications, physical infrastructure and high tech, especially semiconductors and especially when the acquirer is a Chinese company. Firms considering investments in these sectors in Europe would be wise to review the extent of the U.S. assets that would be involved in the transaction. Firms investing in any U.S. business that could be considered to be engaged in "critical technologies" should also investigate whether their investments are subject to a mandatory filing or declaration under the new rules outlined above.

Conclusion

Foreign investors must undergo screening of their envisaged cross-border acquisitions as early as possible in the transaction process.

Recent regulatory developments highlight the ever-increasing need for investors to carefully weigh the potential impacts of applicable foreign investment review mechanisms with the assistance of legal counsel. This would involve, in particular:

- identifying the countries where a foreign investment screening applies and its extent, specifically in relation to the scope and structure of the envisaged transaction,
- clarifying whether the target is involved in any activity/sector (i.e. strategic sensitive sector) which may require prior clearance,
- taking into account the length of screening procedures within the transaction timetable,
- identifying relevant concerns which may arise and proposed solutions, as well as any potential undertakings,
- offering to meet with the national authorities to explain the rationale and details of the envisaged transaction, as well as negotiate with them, and
- drafting the appropriate legal provisions in the transaction documents.

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THIS NEWSLETTER IS INTENDED ONLY AS A GENERAL DISCUSSION OF THESE ISSUES. IT SHOULD NOT BE REGARDED AS LEGAL ADVICE. WE WOULD BE PLEASED TO PROVIDE ADDITIONAL DETAILS OR ADVICE ABOUT SPECIFIC SITUATIONS IF DESIRED. IF YOU WISH TO RECEIVE MORE INFORMATION ON THE TOPICS COVERED IN THIS PUBLICATION, YOU MAY CONTACT YOUR USUAL SHEARMAN & STERLING REPRESENTATIVE OR ANY OF THE FOLLOWING SHEARMAN REPRESENTATIVES AND, FOR SPAIN, JOSÉ MARÍA DE PAZ OF PEREZ-LLORCA:

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