

Foreign Direct Investment (FDI) Control



FDI Control is Catching up to Merger Control

Recent trends in Foreign Direct Investment (FDI) control regimes resemble developments in merger control in the 1990s. More and more countries introduce regimes, ramp-up enforcement and assume jurisdiction over global transactions. Where existing regimes are in place, they tend to be extended, like in the US where the CFIUS regime was broadened under the Trump administration, with no signs that the policy will be reversed. The UK's FDI regime is even stricter than its merger control regime, requiring mandatory notifications where the latter is based on voluntary filings. In the EU, FDI control is essentially national and EU harmonisation is limited to common minimum standards and information exchange. New regimes appear in Asia, notably in China.

It does not require a lot of foresight to predict that M&A counsel around the world will have to start thinking about FDI control in the same terms as merger control – a major factor to be taken into account when assessing deal certainty and deal timing.

Scope of FDI Regimes – No Longer Limited to Military and Defence

FDI has a broad scope of application that differs from country to country. The following serve as an illustration (being the areas where we have had to make filings or advise on FDI control):

- 3-D printing
- Advanced polymers
- Aerial imagery and mapping
- Aerospace
- Food distribution
- Aluminium
- Autonomous vehicles
- Chemicals
- Composites
- Cybersecurity
- Data centres
- Defence
- Electric vehicles
- Electromechanical components
- Energy
- Health care
- Manufacturing automation
- Media
- Precision manufacturing
- Semiconductors
- Telecommunications



FDI control vs Merger Control – Key Differences at a Glance

	FDI Control	Merger Control
Timing	Even unproblematic cases take significant amount of time (e.g US - three to five months; Germany and Spain – up to six months). Phase II investigations are frequently opened as authorities are overwhelmed, not necessarily because of concerns.	Relatively short in unproblematic cases (e.g., US- four weeks; EU – 25 working days plus pre-notification; Germany– one month). Only China typically generates timing issues. Cases with substantive issues can take significantly longer.
Which transactions?	Acquisitions of share capital/voting rights as low as 10% in Germany or Spain. Only foreign buyers are affected in EU member states (exception: UK); this means, outside pure defence, typically non-EU buyers (exception: France).	Acquisitions of control (via share capital or voting rights). Acquisitions of minority shareholdings are rarely caught (notable exception: Germany > 25%). Buyer nationality is irrelevant.
Which industries?	No universal rule: very broad scope in the US, broad scope in UK, much narrower scope in EU Member States.	All.
Is filing mandatory?	No universal rule. In the US, broad scope is counterbalanced by many filings being voluntary. In EU Member States, filings are often mandatory, but the industry scope is often narrower. In the UK, filing is mandatory in identified key sectors.	Typically yes. Parties must not close before approval by all applicable authorities worldwide. The notable exception is the UK, where filing is voluntary.
Jurisdictional trigger point	Typically requires local acquisition (notably exception: UK); no <i>de minimis</i> sales threshold required.	Typically based on commercial activity within a country, e.g. turnover or market share thresholds; no local physical presence required.
Predictable outcome?	Decisions depend on national policies and are politically, rather than economically, motivated. Policies can be diametrically opposed, e.g. a UK company buying a business with activities in the US and China.	Normally yes, review is based on economics with well-established theories of harm. Often the same issues will arise globally, or at least within a region.

US – The Most Advanced Jurisdiction in FDI Control

CFIUS

The role of CFIUS is to examine the potential national security risks associated with the proposed foreign investment into the US. If the committee determines a transaction would be against the national security interests of the US, CFIUS will work to mitigate the threat, if possible, or recommend to the President that he block the transaction or force divestiture for complete transactions. The Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA) both expanded CFIUS authority and reaffirmed the US commitment to “foreign investment, consistent with the protection of national security policy”.

What Any Deal-Maker (and Deal Lawyer) Needs to Know About CFIUS

CFIUS is authorised by statute to review the US national security implications of “**covered transactions**”.

- Covered control transactions – Any transaction that could result in “control” of a US business by a foreign national, foreign government or foreign entity.
- Covered investments – Any transaction that would result in an acquisition by a foreign person of a non-controlling equity interest in a TID US business.
- Covered real estate transactions – Any transaction resulting in the acquisition of real property rights by a foreign person in certain airports, ports, or near specific military or government facilities listed in the regulations.

Mandatory filings to the CFIUS are required if:

- Any covered transaction involves an acquisition of equity in a US critical technology business (even if the interest is non-controlling under certain circumstances)
- A covered transaction involves a 49% or greater interest acquisition in a TID US business and a foreign government (other than from an excepted state) holds a substantial interest (greater than 25%) in the foreign investor

Voluntary filings:

Parties to any covered transaction have the option of submitting a voluntary filing to CFIUS, which can establish a safe harbour for the transaction to avoid the risk of future CFIUS review, even years after closing.

Whether a transaction triggers a mandatory filing or parties have decided to submit a voluntary filing, parties have the option to submit a long-form notice filing or a short-form declaration filing. The short-form filing is quicker and has no filing fee; however, it is not advisable unless the investment presents little to no concerns.



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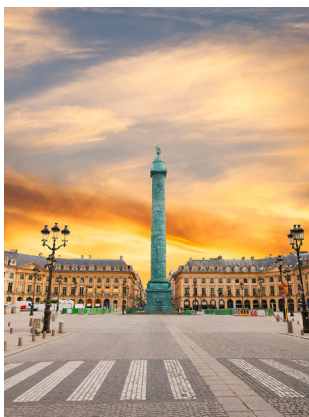
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EU

- **No direct authority** to approve or reject proposed investments; coordination role, but member states retain decision-making power (15 of 27 have national security review mechanisms in place)
- Member states are **required to notify the European Commission and other states** of ongoing FDI reviews, which may include a list of other states whose security or public order are deemed likely to be affected



France

- **Scope** – Public policy and security, defence, media, food, agriculture, energy, water supply, health care, transport, space operations, communications, cryptology resources, critical technologies such as biotechnology, energy storage or quantum technologies.
- **Trigger** – Following transactions (i) taking control of a French company; (ii) acquisition of all or part of a branch of activity of a French company; and (iii) acquisition of more than 25% (threshold temporarily lowered to 10%) of voting rights of a French company (applicable to non-European investors only).
- **Filing mandatory?** – Yes, the transaction must not close before approval.
- **Timing** – 30 business days, extendable by 45 business days.



Germany

- **Scope** – In principle, all sectors but there are special rules for defence, IT security companies, essential infrastructure and (currently planned) a wide range of critical technologies.
- **Trigger** – Acquisition of more than 10% of voting rights for defence, IT security, essential infrastructure (e.g. electricity, telecoms, essential medicines, medicinal products, etc.) and (currently planned) a wide range of critical technologies, such as artificial intelligence (AI), automated driving or flying, industrial robots, semiconductors, IT products and components for server security, nuclear technology, quantum technology, network technologies and 3D printing components; other sectors more than 25% of voting rights.
- **Filing mandatory?** – Yes, the transaction must not close before approval, where required.
- **Timing** – Up to 2 months for Phase I and up to 6 months for Phase II.

EU



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UK

In November 2020, the UK government announced a new NSI regime under which certain direct foreign investments in the UK will require mandatory notification to, and prior approval by, the Department for Business, Energy & Industrial Strategy (**BEIS**) before completion. The mandatory notification requirements will come into force once the NSI Bill is enacted, which is expected some time in 2021.

This new regime also enables BEIS to “call in” retroactively deals (within six months of becoming aware of them) that fall outside the mandatory notification requirements, but which it deems still to raise potential national security risks. BEIS will also be able to look backwards at deals that closed within five years, so long as they closed on or after 12 November 2020.

- **Scope** – any acquisition relating to a UK entity (or an entity carrying out activities in the UK or supplying services/goods to customers in the UK) (**qualifying entity**) or an asset used in connection with activities carried out in the UK or the supply of services/goods to customers in the UK (**qualifying asset**).
- **Trigger** – the acquisition of (i) either more than 15%, 25%, 50% or 75% of votes or shares, (ii) voting rights that enable or prevent the passage of any class of resolution, (iii) material influence over policy relating to a qualifying entity, or (iv) a right or interest in, or in relation to, a qualifying asset which enables the use of it or direct control over its use.
- **Filing mandatory?** – Yes, the transaction must not close before approval for triggers (i) – (ii) above if the acquisition relates to one of 17 key sectors (including the energy, communications and transport sectors) or it will be declared legally void. Parties are otherwise encouraged to self-assess whether voluntary notifications should be made for any other trigger (regardless of whether they relate to one of the 17 key sectors).
- **Timing** – initial screening of mandatory or voluntary filings (30 working days); full national assessment (30 working days, extendable unilaterally by BEIS by 45 working days, further extendable by agreement with the parties).



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Poland

- **Scope** – Energy, defence, national security and telecommunications. Due to COVID-19, there are also provisions in place until 25 July 2022 to protect entities in critical infrastructure, financial services, food and water supply, data storage, health care, laboratories and transport.
- **Trigger** – Direct or indirect acquisition of more than 20% of votes in the target.
- **Filing mandatory?** – Yes. If the transaction takes place before the filing is made and clearance obtained, it is null and void and the parties may be subject to penalties.
- **Timing** – 90 days, then 30 business days for Phase 1 and 120 days for a Phase II investigation.

Poland



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Italy

- **Scope** – Energy, transport, communications, defence, national security and 5G; recently extended to “high-tech” companies (technology intensive activities), such as those dealing with data, AI and robotics.
- **Trigger** – Depends on the sector; for example, energy, transport, communications: (i) resolutions, acts or transactions leading to a change of ownership or control of the company’s assets, e.g. merger; and (ii) relevant acquisitions (defined as the ability to determine a permanent establishment of the buyer into the company).
- **Filing mandatory?** – Yes, the transaction must not close before approval.
- **Timing** – Filing 10 days from signing; review period of 30 to 45 days. The Italian government may extend the review period by requesting additional information from the parties.



Spain

- **Scope** – Physical or virtual critical infrastructures, critical technologies and dual use items, supply of essential inputs, sectors with access to sensitive information and the media.
- **Trigger** – More than 10% of the total share capital of a company.
- **Filing mandatory?** – Yes, the transaction must not close before approval.
- **Timing** – Up to six months.



Czech Republic

- **Scope** – Infrastructure, energy, food and agriculture, transport, health care, telecoms and data, financial services, media, defence (including dual-use), and other sectors where the investment is of national security concern.
- **Trigger** – Any investment that establishes (i) control of at least 10% of voting rights, (ii) membership in the target, (iii) right of disposal of proprietary rights to property used for economic activity, or (iv) any other degree of control that allows the investor access to information, systems or technology essential for the protection of national security.
- **Filing mandatory?** – Yes. Sanctions include fines and mandatory divestment.
- **Timing** – Up to seven months, perhaps longer depending on the transaction risk.

Italy



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China

- **Scope** – (i) All types of investment (including greenfield), and (ii) defence, agricultural products, energy, major equipment manufacturing, infrastructure, transport, culture, technology and internet, financial services, key technologies, and other essential industries of national security concern. All must be critical in nature.
- **Trigger** – (i) Defence-related: any investment; (ii) other sectors: actual control by foreign investors.
- **Filing mandatory?** – Yes, the transaction must not close before approval.
- **Timing** – Preliminary Review (15 business days), General Review (30 working days) and Special Review (60 working days).

China



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Australia

- **Scope** – In principle, all sectors but there are special rules that apply to foreign government investors (FGIs) in specific industries, including agribusiness, critical infrastructure (businesses that hold assets such as electricity, gas, water or ports), telecommunications, critical military-use goods or intelligence technology, critical defence services, critical defence information and certain categories of land.
- **Trigger** – Acquisition of a substantial interest (20% or more) in an Australian entity, direct interest (10% or more, or in a position to control or influence) in Australian land or agribusiness, any acquisition by an FGI and “notifiable national security actions” (for which there are different percentage triggers depending on the sector).
- **Filing mandatory?** – Yes, the transaction must not close without Foreign Investment Review Board (FIRB) approval (financial and criminal penalties may apply).
- **Timing** – Deadline of 40 days (including 30 days for the Treasurer to make the decision and a further 10 days to notify the applicant of the decision). The Treasurer has powers to extend the decision period for up to 90 days.

Australia



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Japan

- **Scope** – Acquisitions of, investments in, loans to, the establishment of, and certain actions with respect to a Japanese entity.
- **Trigger** – Very broad thresholds; virtually any acquisition of shares, acquisition of voting rights and certain acquisitions of securities.
- **Filing mandatory?** – Yes. The transaction can be unwound if it relates to a designated industry (Core Restricted Businesses) and closes or the action is taken before approval.
- **Timing** – 30 days in principle; however, this can be shortened to two weeks or, in some cases, just four days. If an examination for national security is required, the period can be extended for up to five months.

Japan



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Special Focus on UK

Interview With Matthew Kirk

Q: In a country where merger control is voluntary, is this a game changer?

A: I think it is, for two reasons. First, simply in terms of workflow, this new legislation vastly increases the number of transactions likely to be scrutinised – from an average of less than one per year over the previous 18 years to anything up to 1,000 a year under the new regime. Second, it is quite a change of philosophy. The UK has traditionally been one of the most open markets to foreign capital with very few barriers to foreign ownership. The government has denied that this legislation marks a change to that, but it certainly puts significantly more process and control into many M&A transactions.

Q: What are the substantive criteria for review?

A: The law sets some (very low) thresholds, and some (fairly broad) sectors are covered but it also has some catch-alls, such as being a supplier to government irrespective of sector. It does not, however, precisely define the framework against which a transaction might be reviewed. The Statutory Instrument gives a more detailed framework, with 17 schedules of sectors and activities which are in scope. Some of the schedules give very detailed parameters, but others are less well defined leaving more open to judgement. The good news is that the legislation is grounded in the national security interest (which is broad, but has a clear rationale), as opposed to national interest, which can really encompass more or less anything.

Q: Already, merger control introduces deal uncertainty. How is this different?

A: Merger control is, to a large extent, predictable – if you hire the right law firm and economic modellers, you can work out where your problem areas will be and, therefore, have a strategy to address them from the start, even before you have launched your bid for the M&A target. With national security screening, you get two more subjective factors. First, a lot of the input into the decision will come from security agencies whose interests and working methods are not generally publicly known, so you start from a position of uncertainty against what policy priorities your deal will be evaluated. Second, there is likely, in at least some cases, to be a “national champion” element.

Q: Is there a higher level of politics involved?

A: Correct. In FDI control, the stakes are much more political. It is not hard to see that the foreign subsidiary of a bicycle manufacturer is relatively unlikely to come under scrutiny, whereas a UK-owned maker of nuclear control systems is virtually certain to. Between those, there will be hundreds of companies in respect of which the position is much less clear, and for which other factors are certain to influence the decision. People advising on mergers and takeovers will need to be able to offer an understanding of the UK national security framework and an almost intuitive reading of the politics of a proposed transaction, neither of which is part of the traditional offering.

Q: Given the similarities of approach to the US, will US precedents help?

A: To some extent, yes. Certainly, the structures used in order to secure CFIUS clearances will provide a model for the UK. But I think it would be unwise to assume that because something has not required scrutiny under CFIUS, the same will be true of the UK (and vice versa). The politics and the perception of national security interest could well be different. And it does not stop with the US: there are more and more slightly different regimes with different political and national security considerations behind them, so managing a multicountry M&A project is becoming ever-more complex.



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Assessing the FDI Risk of the Transaction

The following business factors, if present, would increase the risks that FDI authorities could be concerned about some or all of the covered transaction.

Maintaining or Collecting Personal Data

- Produce, design, test, manufacture, fabricate or develop one or more critical technologies
- Own, operate, service or key supplier to critical infrastructure (e.g. energy)
- Sole source, or one of only a few qualified sources, that directly or indirectly supplies any agency of the US government
- Involvement in the defence industry, products or technology with current or anticipated military applications
- Operations of the business involved in evolving areas of high risk, such as advanced semiconductor R&D; services/ software business that has access to other companies' data or facilities; or integral to food or medical supply chains (exacerbated by COVID-19)

Foreign Investor Risk Factors

- Foreign investor is from a jurisdiction that is geopolitically adverse to policy
- For investors from allied countries, whether the foreign investor has material commercial relationships with countries or entities adverse to policy (e.g. business with countries subject to US sanctions), even if those relationships are lawful
- For non-Chinese investors, whether the foreign investor has a significant presence in China or business relationships with Chinese entities
- Any criminal or regulatory violations, such as export control or anticorruption violations

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