

EU Adopts Regulation on Foreign Direct Investments

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On March 19, 2019, the European Union adopted a regulation for the screening of foreign direct investments into the EU (the Regulation).¹ The Regulation sets forth national security factors that EU member states (Member States) and the EU Commission (the Commission) may consider when assessing foreign direct investments by non-EU investors. The Regulation entered into force on April 10, 2019, and will have direct effect in Member States from October 11, 2020. This transitional period is meant to enable Member States and the Commission to put in place tools and resources in place to fully apply the Regulation.²

Background and Approach

In September 2017, the Commission's president, Jean-Claude Juncker, unveiled an initial proposal for an EU regulatory framework on foreign direct investments during his State of the Union address. In his speech, President Juncker placed particular emphasis on foreign state-backed acquisitions of European infrastructure and key technology. After extensive discussions and consultation, the European Parliament, Council and Commission eventually reached an agreement on a legal framework for screening foreign direct investments in November 2018, clearing the way for the Regulation to be adopted.

The Regulation takes a very cautious approach: It does not set up a centralized screening mechanism at the EU level (Member States that have screening mechanisms in place will continue to screen foreign direct investments at the national level); it does not grant any approval or veto powers to the Commission; it does not require Member States to put in place a foreign investment screening mechanism if they do not already have one (Member States have sole responsibility to decide whether to screen foreign direct investments); and Member States are free to decide the type of screening procedure to implement — notably, they can choose whether to implement a prior authorization regime or an *ex post* screening mechanism.

The Regulation

The main purpose of the Regulation is to create a legal framework for screening foreign direct investments that may affect security or public order in the EU, and to establish a cooperation mechanism among Member States and the Commission in this field.

Scope

The Regulation covers only investments by non-EU investors in the EU and does not extend to intra-European foreign investment flows. The Regulation broadly defines foreign direct investment as:

“an investment of any kind by a foreign investor that aims to establish or maintain lasting and direct links between the foreign investor and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry out an economic activity in a Member State, including investments that enable effective participation in the management or control of a company carrying out an economic activity.”

¹ Regulation 2019/452 of March 19, 2019, establishing a framework for the screening of foreign direct investments into the EU, 2019 O.J. (L 79)1.

² See Skadden client alerts, “[Foreign Investment Control Reforms in Europe](#)” (Jan. 17, 2019) and “[Expanding the Scope of National Security-Focused Foreign Investment Reviews in Europe](#)” (July 2, 2018).

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Each Member State is responsible for establishing the appropriate criteria, through national legislation, for transactions that may qualify as foreign direct investments pursuant to their national law (e.g., acquisition of control, ownership thresholds, influence on sensitive activities or industries, etc.).

Screening Factors and Process

The Regulation covers foreign direct investments that are likely to affect security or public order interests. The Regulation does not, however, provide a general definition of national security. Instead, the Regulation provides a list of non-exhaustive factors that Member States or the Commission may consider when determining whether a foreign investment is likely to affect security or public order. These factors relate to the potential effects of the foreign investment on, among other things, critical infrastructure,³ critical technologies and dual-use items,⁴ supply of critical inputs,⁵ access to or the ability to control sensitive information,⁶ and the freedom and pluralism of the media.

Additionally, the Regulation provides that Member States and the Commission may consider, among other things, whether the foreign investor is directly or indirectly controlled by the government of a third country through ownership or significant funding. Member States and the Commission also may consider whether the foreign investor had already been involved in activities affecting security or public order in a Member State, or if there is a serious risk that the foreign investor engages in illegal or criminal activities.

The Regulation requires that rules and procedures governing foreign direct investment screening mechanisms are transparent and do not discriminate between third countries. Member States are required to set out the circumstances that trigger the screening, the grounds for the screening and the applicable detailed procedural rules. Additionally, Member States must apply specific timeframes under their screening mechanisms and must give the possibility to foreign investors and concerned entities to seek recourse against screening decisions. Lastly, screening Member States are required to ensure the protection of confidential information (including commercially sensitive information) made available to them as part of the screening process.

³ Whether physical or virtual, including energy, transport, water, health, communications, media, data-processing or storage, aerospace, defence, electoral or financial infrastructure, and sensitive facilities, as well as land and real estate crucial for the use of such infrastructure.

⁴ Including artificial intelligence, robotics, semiconductors, cybersecurity, aerospace, defence, energy storage, and quantum and nuclear technologies, as well as nanotechnologies and biotechnologies.

⁵ Including energy or raw materials, as well as food security.

⁶ Including personal data.

Cooperation Mechanism; Exchange of Information

The Regulation establishes a cooperation mechanism among Member States and the Commission when a foreign direct investment in a Member State could potentially affect security or public order in another Member State.

1. Under the Regulation, Member States must notify the Commission and other Member States of any foreign direct investment that is undergoing screening in their territory.
2. If a Member State considers that a planned or completed foreign direct investment in another Member State (regardless of whether such investment is undergoing screening in such Member State) is likely to affect its security or public order, or has relevant information related to that foreign direct investment, the Member State may provide comments to the Member State in which the relevant investment is planned or has been completed.
3. If the Commission considers that a planned or completed foreign direct investment in a Member State's territory is likely to affect security or public order in more than one Member State, or has relevant information related to such foreign direct investment, the Commission may issue an opinion to the Member State receiving the investment regardless of whether other Member States have provided comments. Additionally, the Commission is required to issue an opinion if at least one-third of Member States consider that a foreign direct investment is likely to affect their security or public order.
4. A Member State that reasonably considers that a foreign direct investment in its territory is likely to affect its security or public order may request the Commission to issue an opinion or other Member States to provide comments.
5. The Commission and Member States have certain information rights vis-à-vis the Member State where a foreign direct investment is planned or has been completed. The Regulation includes a list of information that such Member State is required to provide, which includes, among other things, relevant information on the foreign investor and the investment.⁷ Under the Regulation's cooperation mechanism, relevant information that is shared among Member States and the Commission is centralized at the level of the Commission.

⁷ The required information includes: (a) the ownership structure of the foreign investor and of the undertaking in which the foreign direct investment is planned or has been completed, including information on the ultimate investor and participation in the capital; (b) the approximate value of the foreign direct investment; (c) the products, services and business operations of the foreign investor and of the undertaking in which the foreign direct investment is planned or has been completed; (d) the Member States in which the foreign investor and the undertaking in which the foreign direct investment is planned or has been completed conduct relevant business operations; (e) the funding of the investment and its source (on the basis of the best information available to the relevant Member State); and (f) the date when the foreign direct investment is planned to be completed or has been completed.

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6. The Regulation includes certain deadlines in the cooperation mechanism among Member States and the Commission. The deadlines vary, depending on whether the foreign direct investment is undergoing screening in a Member State:
 - a. If a Member State or the Commission considers that a foreign direct investment undergoing screening in another Member State is likely to affect security or public order interests, the concerned Member State or the Commission is required to notify the screening Member State of their intention to provide comments or an opinion no later than 15 calendar days after being notified of the investment.⁸
 - b. In cases where a planned or completed foreign direct investment is not undergoing screening, a Member State or the Commission may provide comments or issue an opinion on such investment to the relevant Member State, no later than 15 months after the foreign direct investment has been completed, if they consider that such investment is likely to affect security or public order.⁹
7. The Regulation provides that, when a Member State receives comments from other Member States or an opinion from the Commission, it must give due consideration to such comments or opinion. Screening Member States, however, shall retain final decision powers regarding the screening of foreign direct investments in their respective territories.

Projects or Programs of EU Interest

Under the Regulation, if the Commission considers that a foreign direct investment is likely to affect projects or programs of EU interest on grounds of security or public order,¹⁰ the Commission may issue an opinion addressed to the Member State where

⁸ Additionally, for investments undergoing screening, if the concerned Member State would like to provide comments, or if the Commission would like to issue its opinion, they are required to do so no later than 35 calendar days after the screening Member State provides information related to the foreign investment. Moreover, if the concerned Member State or the Commission requests additional information from the relevant Member State, their comments or opinions must be issued no later than 20 calendar days following receipt of the additional information or the notification.

⁹ Additionally, if the concerned Member State or the Commission requests information related to the foreign direct investment and the relevant Member State provides such information, the concerned Member State or the Commission has up to 35 calendar days after they have received the information to provide comments or issue an opinion to the relevant Member State. The Regulation grants the Commission 15 additional calendar days to issue an opinion, if such opinion will be issued after the concerned Member State has provided comments.

¹⁰ Projects or programs of EU interest shall include those that involve a substantial amount or a significant share of EU funding or that are covered by EU law regarding critical infrastructure, technologies or inputs that are essential for security or public order. The Regulation includes a list of such programs (e.g., Galileo, EGNOS, Copernicus, Horizon 2020, Trans-European Networks for Transport (TEN-T) and Trans-European Networks for Energy (TEN-E)).

the relevant investment is planned or has been completed. The Commission also shall send its opinion to the other Member States. The Member State where the foreign direct investment is planned or has been completed shall take utmost account of the Commission's opinion and provide an explanation to the Commission if it does not follow the opinion.

Annual Reporting

By March 31 of each year, Member States must submit an annual report to the Commission covering the preceding calendar year, which includes aggregated information on foreign direct investments that took place in their territories, as well as aggregated information on requests received from other Member States in connection with the European cooperation mechanism. Additionally, Member States that maintain screening mechanisms are required to provide aggregated information on how they applied their screening mechanisms.

The Commission is also required to publish an annual report on the implementation of the Regulation to the European Parliament and the European Council.

Anti-Circumvention Measures

Under the Regulation, Member States that have a screening mechanism in place are required to maintain, amend or adopt necessary measures to identify and prevent circumvention of the screening mechanisms and decisions.

International Cooperation

The Regulation provides that Member States and the Commission may cooperate with the responsible authorities of third countries on issues related to the screening of foreign direct investments on grounds of security and public order.

Brexit Implications

In light of the ongoing Brexit negotiations, there is a degree of uncertainty regarding if and how the Regulation may impact the United Kingdom's approach to foreign investment review.

1. In the event of a "no deal" Brexit, the Regulation would not apply to foreign investment flows into the U.K.. In this scenario, it is unlikely that the U.K. would participate in the Regulation's cooperation mechanism and disclosure requirements, or share highly sensitive information, both for security and commercial reasons. The Regulation would, however, apply to investments into the EU by U.K. investors. The U.K. government has indicated that it may voluntarily work with other countries on a case-by-case basis on foreign investment matters.

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2. If the U.K. ratifies the draft Agreement on the Withdrawal of the United Kingdom from the European Union or agrees to an alternative deal that includes a transitional period, the U.K. would continue to be a Member State of the EU during such transitional period and would therefore be obliged to comply with the Regulation. The U.K. government has indicated that it does not, however, expect the Regulation to substantially affect the U.K.'s approach to foreign investment review or have a dramatic impact on inbound foreign investment flows into the U.K. Additionally, the U.K.'s involvement in the EU-wide cooperation mechanism will be subject to the outcome of the negotiations for the Future Economic Partnership.¹¹

Independently of the Regulation, the U.K. government has recently conducted public consultations on proposed changes to the U.K.'s national security screening regime, which, if enacted, would constitute a significant expansion of the government's powers to intervene in transactions on national security grounds. The tentative expectation is that the new regime will come into force by the end of 2020.

United States/CFIUS

CFIUS reform adopted in 2018¹² specifically tasked the U.S. government to engage allies in developing their own foreign direct investment review program, an effort led by the U.S. Department of the Treasury that is underway and will likely align with key aspects of the Regulation, such as increased information sharing.

¹¹ The Future Economic Partnership refers to the ongoing discussions and negotiations between the EU and the U.K. on the political framework of their future relations, after the U.K.'s withdrawal from the EU.

¹² See Skadden client alert, "[US Finalizes CFIUS Reform: What It Means for Dealmakers and Foreign Investment](#)" (Aug. 6, 2018).

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Independent of nascent EU-driven coordination, informal coordination amongst states — as illustrated by U.S.-German cooperation regarding China's Fujian Grand Chip Investment Fund's failed acquisition of Aixtron — requires a holistic approach to any cross-border investment that implicates sensitive industries or information.

Key Takeaways

Key takeaways from the Regulation are:

- foreign investors should be aware of the Regulation's focus on investments in strategic sectors, key technologies and critical infrastructures;
- the Regulation does not grant veto rights to the Commission, but its provisions enable the Commission to exercise significant influence on decisions that Member States will take on foreign direct investments;
- the Regulation may lead to a more burdensome review process and longer review periods for foreign direct investments at the Member State level, in order to comply with the requirements and timelines included in the Regulation's cooperation mechanism;
- the Regulation may open the door for deeper communication and cooperation on national security matters between Member States, the Commission and non-EU authorities (e.g., the Committee on Foreign Investment in the United States (CFIUS)); and
- the Regulation leaves significant flexibility to Member States. It therefore is critical that non-EU investors looking to invest in strategic or sensitive activities across Europe assess at the outset of the deal the institutional specificities and policy approach of the relevant Member States with respect to foreign investment control.