The Evolving Global Foreign Direct Investment and National Security Review Landscape

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Executive Summary

The national security and foreign direct investment ("FDI") review landscape around the world is evolving rapidly. A pre-pandemic trend of active FDI reviews in countries around the world has gained momentum and resulted in the emergence of new FDI regimes. Not only have new FDI regimes proliferated, but also there has been a tightening of existing regimes with an ever-growing number of market sectors viewed as strategically important and thus subject to heightened scrutiny. These trendlines have converged with a surge in global dealmaking, adding to regulatory complexity and resulting in a growing list of deals that need to navigate potential FDI and national security concerns. It is thus more important than ever to evaluate FDI screening risks early in the due diligence process, giving careful consideration to the risks and threats posed by buyers, investors and targets and to potential substantive (mitigation conditions) and procedural (timing) implications. In the following sections, we contextualize these trends in a focused set of jurisdictions to assist cross-border dealmakers with understanding the headwinds and assessing how best to manage FDI-related considerations from the start of the transaction process so as to avoid impediments to closing.

Global deal flows broke recent records in 2021, surpassing the USD 5 trillion mark. Data from the United Nations Conference on Trade and Development indicates global FDI has exceeded pre-pandemic levels, up 77% in 2021 to approximately USD 1.65 trillion. This occurred in a climate of protectionist sentiment complicated further by new and increasingly complex FDI review regimes around the world. The COVID-19 pandemic, too, has disrupted global supply chains and devastated international trade, even as the need to raise capital remains high.

While only about one-third of all countries have some form of FDI screening regulations, about 90% of the 38 Organisation for Economic Co-operation and Development ("OECD") member countries have such regimes (compared with 60% a decade ago).

Major economies have become more focused on safeguarding national security by maintaining economic and technological sovereignty

This has resulted in an expansion of authority for existing national security review regimes and an ever-expanding list of sectors that are subject to scrutiny. The Committee on Foreign Investment in the United States expanded its already broad review authorities in a number of areas, including transactions that involve U.S. sophisticated technology, personal data, and infrastructure. The French Ministry of Economy and Finance, in charge of approving foreign direct investments into strategic sectors, recently issued its first guidelines, intended to make the process of FDI in France more transparent. Other countries including Australia are taking steps to expand their review processes or are considering doing so. Globally, FDI regimes are increasingly scrutinizing sensitive sectors like the semiconductor industry and are looking closely at the vulnerabilities of supply chains.

All content in this publication is up to date as of May 2022, except the France chapter which has been updated since then to reflect the French guidelines issued in September 2022.

In this climate, and with the encouragement of the United States, the EU and many of its Member States have developed or enhanced approaches to screening FDI. China, too, has developed an FDI review framework, possibly in response to increased scrutiny of Chinese investors under U.S. and European regimes. And Russia has drastically altered its approach to FDI in response to economic sanctions and export control restrictions imposed on Russia in view of the situation in Ukraine.

The rise in FDI regimes coupled with the recent rebound in FDI volume means that cross-border transactions are increasingly complex from a regulatory perspective. FDI screening may be impeding deals and constraining the ability of some investors to put capital to work. In 2021, withdrawn global M&A deal volumes reached approximately USD 700 billion, surpassing 2020, 2019, and the five-year average, likely due to regulatory headwinds.

The policy space around FDI review is maturing, but it is not doing so uniformly. Instead, a patchwork of regimes has developed with varying degrees of sophistication. Looking to the future, we can expect to see regimes becoming more detailed and sophisticated in their design as jurisdictions fine-tune their rules. There will be modifications of policies or practices that will increase the number of areas of the economy that are considered sensitive for national security purposes, such as technology and healthcare. And there is the possibility of international cooperation and convergence, as we have seen with respect to the United States' coordination with Australia, the UK, and others, and the EU's coordination across Member States.

FDI is facing an increasingly complex regulatory landscape as screening regimes proliferate

These regulations often cast a wide net: there are multiple FDI regimes which feature a broad jurisdictional nexus which means that even relatively small transactions may be captured as well as investments involving limited governance and control rights. Both buyers and sellers can undertake due diligence to evaluate potential national security regimes that are implicated by proposed transactions and take steps to mitigate potential risks voluntarily before presenting transactions to regulators. Such steps can help parties obtain regulatory approvals and clearances on their preferred timeline and reduce the risk that their transactions become cautionary tales.

Dechert regularly advises foreign and domestic entities through the FDI review process, helping them determine if they should bring a transaction before the review body, consider the political and policy considerations that may arise, assemble the required information for a filing, and then (as necessary) negotiate with the review body in a manner that minimizes both delay and the imposition of conditions that might threaten the transaction.

Australia

Key Considerations

- Recent changes to the Foreign Investment Review Board ("FIRB") FDI regime have resulted in an expansion of FIRB's jurisdiction.
- These changes add complexity to the FIRB review process and reinforce the importance of considering FIRB implications early on for Australian investment targets.
- Private equity funds with non-Australian investor participants should also consider whether they qualify for the new Foreign Government Investors ("FGI")-related exemption, which could result in certain private equity transactions no longer being subject to FIRB review.

FDI Regime Overview

Foreign investment has been a key component to the development of Australia's economy and the FIRB is the governmental agency tasked with ensuring all non-Australian investment proposals are consistent with the country's national interest. In January 2021, the Australian government expanded FIRB's jurisdiction to protect economic sectors deemed essential to its national security. In practice, the reforms have resulted in a greater number of transactions being subject to the FIRB review process, which is described below.

Pursuant to the Foreign Acquisitions and Takeovers Act 1975 (Cth) ("FATA"), non-Australian persons must make an application to FIRB in order to make acquisitions of equity interests in Australia that involve:

- Agribusiness or agricultural land;
- A "substantial interest" (i.e., an interest of 20% or more) in an Australian entity with an enterprise value of AUD 180 million or more; and/or
- Australian land holdings.

When reviewing a potential investment, FIRB will consider the transaction's impact on competition, the economy, the community, and national security, as well as the character of the non-Australian investor.

Recent Changes

Recent changes under the Foreign Investment Reform (Protecting Australia's National Security) Act 2020 (Cth) ("FIR Act") have broadened and strengthened the FIRB review process and created an important exemption for private equity funds. Key aspects of the FIR Act include:

- **The adoption of a mandatory review requirement for acquisitions of interests of any size in a "national security business" and/or "national security land" regardless of their value (i.e., no enterprise value threshold).**

  The definition of "national security business" under the FIR Act includes the following types of businesses: critical defense or intelligence services, critical infrastructure, critical goods or technologies for military- or intelligence-use, sensitive information, and telecommunications. These categories cover broad swaths of the Australian economy. The definition of "critical infrastructure" was also expanded to encompass the following critical infrastructure sectors:

  - Communications;
  - Data storage and processing;
  - Defense;
  - Energy;
  - Food and grocery;
  - Financial services and markets;
  - Health care and medical;
  - Higher education and research;
  - Space technology;
  - Transportation; and
  - Water and sewerage.

- **Timing Considerations: Extension of the 30 days review period up to 90 days at the discretion of FIRB or the Australian government more broadly.**

  Once an application for review has been submitted, FIRB has 30 days to determine whether approval will be granted. FIRB can however extend the review timeline up to 90 total days for a number of reasons, including if additional information is required by FIRB.

In addition, the Australian government can extend the review timeline if it so chooses. During the beginning of the COVID-19 pandemic, on March 29, 2020, the FIRB review period was extended up to six months in order to combat potential threats to Australia's economic security (e.g., investments in distressed businesses and assets). Although the Australian government was quick to assuage investors that FIRB would only take the full six months if absolutely necessary, the temporary change (which ended on January 1, 2021) still allowed FIRB the flexibility of a longer review timeline.

When considering transaction timing, parties should take a conservative approach in estimating the length of FIRB reviews

- **Exemption from the zero-value threshold otherwise applicable to FGI investments for certain private equity funds with FGI.**

  Prior to the FIR Act, an investor was deemed to be an FGI if it was a (i) corporation, (ii) trustee of a unit trust or (iii) general partner of a limited partnership and either:

  - FGIs from one country have a 20% or greater collective interest in the investor; or
  - FGIs from more than one country have a 40% or greater collective interest in the investor.

  As a result, a number of investment funds, in particular private equity funds, were considered to be FGIs if their investors (or limited partners) included FGIs (such as sovereign wealth funds).

  Under the new FIR Act exemption, where an investment fund is an FGI because of FGI participation and where certain 'passive investor criteria' are met (i.e., individual investors are not able to influence investment decisions, or the management of any investments, of the fund), the investment fund is no longer deemed an FGI (or subject to the zero-value threshold). This exemption generally mirrors the private equity exemption to CFIUS jurisdiction in the United States. Unlike in the CFIUS context, however, the Australian exemption is not automatic. Instead, investment funds must apply for the exemption, and FIRB guidance states that applications will be assessed on a case-by-case basis.

Recent Filings Data

In recent years, FIRB has rejected few proposed acquisitions. Based on data available from the 2019-2020 review period, FIRB reviewed 8,224 applications and rejected three. Likewise, during the 2018-2019 review period, FIRB reviewed 8,725 applications, and only one was rejected.

However, parties should always consider that the approval data does not show applications that were withdrawn before the review was completed.

During the 2019-2020 review period, 780 applications were withdrawn from review.

During the 2018-2019 review period, 741 applications were withdrawn from review.

Accordingly, in each of these review periods, approximately 8% of all applications were withdrawn.

In addition, prolonged FIRB reviews have reportedly derailed a number of transactions in recent years.

Recent Trends

Although China is one Australia's largest trading partners, Chinese investment in Australia has fallen in recent years (there were 600 fewer approvals of Chinese investments in the 2019-2020 review period than in the 2018-2019 review period). This is in part because of tighter capital controls by the Chinese government, but it is also a sign of political strain between the two countries. Although full data is not yet available for the 2020-2021 review period, at least four investments have been rejected by the FIRB during this period, including the proposed AUD 600 million sale of Lion Dairy to China Mengniu Dairy Company, and the proposed AUD 300 million sale of Probuild Constructions to China State Construction Engineering Corporation. Importantly, each of these investments involved a business that falls within a critical infrastructure industry (food, construction, and mineral resources), which highlights the significance of the FIRB's recent jurisdictional expansion.

This does not mean that Australia is closed to Chinese investment, however. During the 2019-2020 review period, China was the sixth largest source of approved FDI (AUD 12.75 billion) and accounted for 4,314 approvals out of 9,004 total approvals for the period.

Outlook for 2022

The recent changes to the FIRB's FDI review regime are a significant expansion of the FIRB's powers but also provide important clarifications and relief, including to private equity funds. Although full data is not available from the review period during which the change took effect, the new FIRB review landscape means that parties should think through FIRB implications early on when considering an Australian investment target so that they are prepared to address potential substantive and/or timing-related obstacles.

China

Key Considerations

- China has introduced a number of national security-driven regulations over the last decade, including a revamped foreign investment regime, a foreign investment screening body, and a list mechanism pursuant to which non-Chinese individuals and entities can be restricted or prohibited from investing in China.
- Under the foreign investment regime, a new screening body has broad authority to review both direct and indirect investment activities by non-Chinese investors, including for investments in "important" industries such as energy, infrastructure, and critical technology.
- The newly introduced Unreliable Entity List ("UEL") illustrates China's willingness and ability to target specific actors seen to be endangering Chinese sovereignty or development interests, potentially through compliance with non-Chinese law (e.g. sanctions).
- Non-Chinese investors should continue to anticipate a complex regulatory landscape for investments in China.

FDI Regime Overview

China has introduced a number of national security-driven regulations over the course of the last decade, including several recent measures with respect to non-Chinese investment

First, a new Foreign Investment Law ("FIL") was implemented to overhaul China's foreign investment regime in 2020. The FIL anticipated the Measures on National Security Review of Foreign Investments ("Review Measures"), establishing a new foreign investment screening body in China effective from January 18, 2021, the Authority of the Security Review of Foreign Investments ("Security Review Authority" or "SRA"), led jointly by two of the country's preeminent regulators, the National Development and Reform Commission and the Ministry of Commerce ("MOFCOM"). In addition to these new review measures, MOFCOM also promulgated the Provisions of the Unreliable Entity List ("UEL Provisions") on September 19, 2020, under which non-Chinese individuals and entities so designated may be restricted or prohibited from investing in China.

While these measures directly focus on foreign investment related to China and its interests, it may be helpful to consider them alongside a fuller complement of recent national security-driven measures encompassing cybersecurity, data privacy and data security, anti-foreign sanctions, antimonopoly, export controls, public listing rules and more. We discuss the Review Measures and UEL Provisions below.

Review Measures – Scope of Application

The SRA has broad authority to review both direct and indirect investment activities by non-Chinese investors. Filings with the SRA are required for non-Chinese investments:

- in, or in close physical proximity to, industries associated with the military and national security; and
- where "actual control" is obtained over entities (existing or newly established) in industries designated as "important," including agricultural products, energy and resources, infrastructure, transportation services, equipment manufacturing, information technology, internet products and services, financial services, "critical" technologies, cultural products and services, and "other important fields." "Actual control" refers to (i) holding more than 50% of a target's equity; (ii) holding less than 50% of a target's equity, but with significant voting rights; and (iii) "other circumstances" allowing a non-Chinese investor to have a significant impact on the business decision-making, personnel, finance, and technology of the enterprise. Both the "other important fields" prong of the targeted industries test and the "other circumstances" prong of the actual control test offer the authorities a wide scope of discretion.

Notably, investments in listed companies impacting national security are also subject to review by the China Securities Regulatory Commission ("CSRC") in conjunction with SRA (and regulators have recently released draft national security-driven measures in respect of offshore fundraising and public listings). The Review Measures call for CSRC to develop specific measures with SRA to review such investments

Review Measures – Procedures & Outcomes

SRA filings undergo a multi-stage review with both defined and undefined review stages:

- **Preliminary Consultation (no set timing).** Parties have the opportunity to consult the SRA, but we understand consultation will not result in the issuance of any opinion (formal or informal). The preliminary consultation can inform non-Chinese investors whether they need to make a filing with SRA.

- **Preparation of Required Application Materials (no set timing).** If a filing is deemed required, parties must prepare and submit a declaration form, investment plan, statement on national security impact and any other materials required by the SRA. The SRA will not publicize the existence of a filing, and materials submitted in connection with a filing will be kept confidential.

- **Initial Decision (15 business days).** Within 15 business days, a preliminary decision will be made by SRA as to whether it is necessary to conduct a national security review of the investment. The security review consists of a general review and a special review. If the SRA decides that no security review is required, the parties may move forward with the investment. If not, the parties proceed to the general review.

- **General Review (30 business days).** A general review will be completed by the SRA within 30 business days of the initial decision to conduct a national security review. During a review, the SRA may interview the parties and issue requests for information. The investment will be cleared if it is deemed to not affect national security, otherwise the SRA will notify the parties in writing of a decision to initiate a special review process.

- **Special Review (60 business days, extendable).** – The special review must be completed within 60 business days and may result in either (i) clearance of the investment, (ii) prohibition of the investment, or (iii) conditional approval of the investment. Required conditions will be implemented under the supervision of the SRA and relevant local level authorities. These authorities will also be empowered to conduct on-site inspections to verify compliance. Under special circumstances, this 60 working day review period may be extended by the SRA. Moreover, the SRA may request additional materials from filing parties, and the time taken to provide those materials will not be factored into the statutory review period timeline. The parties may at any time during the review period modify or cancel the proposed investment. If amended, the review period will be recalculated from the date when the SRA receives the revised investment plan from the filing parties. While this issue is not addressed explicitly in the new measures, it is anticipated that decisions of the SRA will be released only to transaction parties and will not be made public. If an approval is conditional the parties will need to implement the investment according to that plan and may need to walk back any actions taken prior to approval. The SRA has the power to extend this 60 business days period for a discretionary length of time.

The Review Measures became effective as of January 18, 2021, and data regarding SRA filings has not been made public.

Unreliable Entity List – Scope of Application

MOFCOM has stated that the UEL is not intended to target any specific country or entity. However, compliance with foreign sanctions against Chinese individuals or entities (or partners) or cooperation with foreign governmental investigations may be important factors in being designated to the UEL. There have yet to be any entries to the UEL or guidance on its implementation and processes. Therefore, the following provides a framework requiring further clarification from regulators.

A non-Chinese entity may be listed on the UEL where it:

- endangers the national sovereignty, national security or development interests of China; or

- suspends normal transactions with or discriminates against Chinese entities in violation of normal market transaction principles and causes serious harm to the legitimate rights and interests of Chinese entities.

Unreliable Entity List – Review Procedures & Penalties

The UEL is to be overseen by a "Working Mechanism" body within MOFCOM and authorized to investigate the actions of a non-Chinese entity based on the following factors:

- the degree of danger to the national sovereignty, security or development interests of China;

- the degree of damage to the legitimate rights and interests of Chinese enterprises, other organizations, or individuals;

- whether it is in compliance with internationally accepted commercial and trade rules; and

- other factors.

Designated entities or individuals may face one or more of the following:

- restriction or prohibition on trading and investing in China;

- restriction or revocation of work permits or residence authorization;

- imposition of monetary fines according to the severity of the circumstances; and

- other penalties or measures at the discretion of the Working Mechanism.

The Working Mechanism will announce entities designated to the UEL including risk alerts of doing business with such entities. Announcements may also provide for curing periods during which the designated entity may take corrective action and the foregoing punitive measures will not be imposed.

Designated entities may apply to the Working Mechanism for removal from the UEL. In addition, the UEL Provisions allow for Chinese entities and individuals to apply for special exemptions where it is necessary for the Chinese applicant to transact with a designated entity. The Chinese party may continue to transact with the designated entity pursuant to the terms and conditions of an issued approval.

The general impression in China is that the Chinese government's purpose in applying the UEL is in response to sanctions imposed by foreign governments

Outlook for 2022

China has issued a raft of sweeping measures over the course of the last several years which will significantly impact non-Chinese investors and the Chinese market as a whole. These have developed against the backdrop of Beijing's long-term policy goals of moving up the technology ladder through industrial policy and rebalancing its economy through increased domestic consumption and self-reliance ("Dual Circulation"). These policies aim to advance the economy while weathering an external environment increasingly perceived to be hostile and avoiding being trapped as a middle-income country.

The country's emerging foreign investment regime is a part of Beijing's broader economic strategy and overall drive to exert national security-based controls over private actors, whether foreign or domestic

For instance, authorities recently released draft measures regarding offshore fundraising ("Overseas Listing Rules"). Dovetailing with the Review Measures, the Overseas Listing Rules strengthen the regulation of Chinese companies listed abroad, including in Hong Kong and for the first time over indirect listings using offshore holding companies as listing vehicles (e.g., "variable interest entities"). Beijing continues to expand national security rationalized protections while further liberalizing the negative lists to court non-Chinese investment in strategic sectors. In the Review Measures we find the country's first truly substantive national security-based foreign investment screening process, while the UEL Provisions illustrate Beijing's increased willingness to impose countervailing pressure against parallel measures coming out of Washington and Brussels. Multinationals and other investors can continue to anticipate novel hurdles to foreign investment and operations in the country. At the same time, the Chinese government appears to recognize the importance of non-Chinese investment to the country and therefore is expected to be judicious with its use of restrictive measures such as the UEL.

European Union

Key Considerations

- The COVID-19 pandemic inspired EU Member States to reinforce existing FDI screening mechanisms and adopt new ones.
- 18 out of 27 EU Member States now have FDI screening regimes, and all Member States are expected to implement them in coming years.
- Statistics for 2020 show Member States intervened in a small proportion of cases, and a significant majority of transactions (80%) were subject to no formal screening, but an uptick in FDI screening activity is expected in 2022.
- Investors will need to navigate a growing patchwork of Member State FDI regimes.
- Due to the prevalence of FDI transactions that involve multiple Member States, the EU appears open to playing a more central role to foster procedural and substantive convergence.

Background

The EU FDI Regulation, which entered into force on October 11, 2020, created a mechanism for coordinating national screening of inward investments by non-EU buyers, while giving the European Commission ("Commission") an important new central advisory role. The entry into force of the Regulation coincided with the second wave of the COVID-19 pandemic, which led multiple Member States to enhance existing FDI screening regimes and/or implement new mechanisms. In addition, those Member States that do not yet have FDI screening mechanisms are expected to introduce them in the short to medium term. The recent geo-political turmoil has almost certainly reinforced the policy imperative to screen inbound FDI.

These developments need to be placed in their wider policy context, notably the EU Industrial Strategy launched at the behest of Member States (with the Franco-German axis leading the charge) following the Commission's veto of the *Siemens/Alstom* merger. In particular, there has been a strong push from Member States to protect the EU's industrial base. This feeds into the wider EU policy objective of achieving "open strategic autonomy"—a concept that "emphasises the EU's ability to make its own choices and shape the world around it through leadership and engagement, reflecting its strategic interests and values." The precarity of global supply chains will have only brought this objective into sharper focus.

> In turn investors can expect to have to navigate an ever-growing patchwork of Member State FDI regimes

which may complicate transaction planning and potentially lengthen timelines. Nevertheless, statements by the Commission suggest that it is acutely aware of the need to achieve some degree of procedural and substantive convergence across the bloc. Indeed, it seems to have already set its sights on the centralization of EU FDI enforcement.

FDI Regime Overview

Although the EU FDI Regulation itself does not require Member States to screen FDI, the European Commission has actively encouraged Member States to set up such regimes and make use of the existing rules, in particular to impede opportunistic buyouts of strategic European assets in the difficult economic circumstances resulting from the COVID-19 pandemic. At the time of publication, 18 of the 27 EU Member States have FDI screening regulations in place, and this this number is expected to increase.

When the EU FDI Regulation entered into force, the existing Member States' systems varied widely in their scope and level of enforcement, and countries did not coordinate their approaches, even where a given investment affected multiple countries (see our OnPoint). The Regulation tries to address this patchwork by specifying a number of characteristics which existing and new screening regulations and mechanisms must meet. It sets out a non-exhaustive list of sensitive sectors Member States may wish to target in their FDI regimes such as aerospace, artificial intelligence communications, defence, energy, financial, media, semi-conductors and transport. The EU FDI Regulation also provides guidance on the types of factors Member States may take into account in their determination of whether an investment is likely to affect security or public order. These include an investor's links to non-EU governments; involvement in activities affecting security or public order; and the risk it may be engaged in criminal or illegal activities.

One of the key features of the EU FDI Regulation is its introduction of a coordination mechanism. This has been achieved through two channels: (i) the facilitation of information sharing between Member States including information on active cases; and (ii) a cooperation mechanism for the Commission and Member States to provide their views and opinions to the Member State(s) screening the FDI. As discussed below, this does not create a one-stop shop comparable to EU Merger Regulation, but there are strong hints that the Commission harbours ambitions to become the FDI ringmaster.

Although the Commission and Member States are able to intervene in ongoing FDI reviews by providing an opinion, this has no binding effect on the reviewing Member State. However, Member States must take account – and in certain circumstances the "utmost account" – of the Commission's opinion. This is the case for targets that receive significant EU funding or operate critical infrastructure (transport, energy, telecoms), produce critical technologies (artificial intelligence, robotics, semiconductors) or manufacture inputs needed for security or public order (cybersecurity, satellite, navigation, earth observation and defense). Nevertheless, different Member States could in theory adopt inconsistent decisions when screening a single transaction.

Review of FDI screening activity

The proliferation of FDI regimes in the EU coincided with a slowdown of inbound FDI into the EU. This trend was called out in the Commission's first annual report on FDI screening in the EU ("EU FDI Report") which was published in November 2021. The drop in EU inbound FDI in 2020 marked two consecutive years of declining FDI levels, which corresponded with an overall drop in global FDI flows. The COVID-19 pandemic exacerbated this downward trend with its impact felt more strongly in the EU when compared to the global average: EU inbound FDI levels fell by 71% in 2020 whereas global FDI flows witnessed a drop of 35%.

Global dealmaking activity has however rebounded strongly since the fourth quarter of 2020 and that trend continued into 2021, surpassing USD 5 trillion in global M&A volume

an all-time record. In the same period, deals involving European targets surged to USD 1.4 trillion hitting a 14-year high. This has translated into a significant uptick in EU inbound FDI levels with OECD statistics for the first half of 2021 recording inflows of USD 109 billion compared to USD 20 billion in same period in 2020. The statistics also show that the EU accounted for over 25% of FDI inflows into OECD countries, which should help to allay fears that the increase in FDI screening in the EU may have a chilling effect on FDI, albeit statistics point to a drop in inbound FDI from China.

The EU FDI Report compiles screening statistics from Member States covering the 2020 calendar year, a timeframe that largely predates the entry into force of the Regulation. The statistics show that investors and their advisers are treading carefully as they familiarize themselves with nascent FDI regimes with 80% of the 1,793 notifications received by Member States subject to no formal screening. This was either because the investments fell outside the scope of the FDI regime or due to an evident lack of impact on security or public order. Member States approved 91% of the cases with 79% cleared unconditionally and 12% subject to conditions. Only 2% of investments were prohibited. The remaining 7% were aborted and thus did not require a decision. Again, the high proportion of clearances is consistent with the stated position of the EU that the bloc remains very open to FDI and that interventions will be limited to a very small proportion of transactions that are likely to pose a threat to security or public order.

As regards notifications submitted to the Commission via the cooperation mechanism (see above), during an approximately nine-month period following the entry into force of the EU FDI Regulation (i.e., 11 October 2020 through 30 June 2021) a total of 265 notifications were submitted. Notifications were made by 11 Member States with Austria, France, Germany, Italy, and Spain accounting for 90% of those notifications. In line with the 2020 Member State FDI screening statistics, 80% of the cases were closed by the Commission in Phase 1. Of the remaining 20% of cases, 14% proceeded to Phase 2 and were subject to additional information requests from the notifying Member State; and 6% of the cases were ongoing at the time the EU FDI Report was being finalised. In terms of sector focus, the Phase II reviews were primarily focused on manufacturing (50%), information and communication technologies (17%) and financial [services] (8%). As for the country of origin, investors from the US, the UK, China, Canada, and the United Arab Emirates accounted for the majority of cases notified to the Commission.

Moreover, the statistics also show that the Commission has so far adopted a relatively light-touch approach in its advisory role: a confidential opinion was issued in less than 3% of the cases notified by Member States. The EU FDI Report underlines that the Commission will issue opinions "only when and if required by the circumstances of a case, more specifically the risk profile presented by the investor and the criticality of an investment target."

Member States' views on the functioning of the EU FDI Regulation

The overall feedback received from Member States was that the EU FDI Regulation and the cooperation mechanism is a "very valuable tool for gaining a comprehensive overview of FDI into the EU, including particular investment targets and investor profiles." In particular, Member States pointed to the ability to ask questions and offer comments to a screening Member State as a positive feature of the Regulation; and highlighted the benefits of formal and informal cooperation including the setting up of the Expert Group made up of Member State and Commission officials.

There have however been some teething problems and some of the procedural issues encountered by Member States included the following:

- **Resource constraints.** Several Member States have experienced resource constraints from a staffing standpoint, especially smaller Member States and screening authorities.

This has been exacerbated by the very tight deadlines (discussed below) and more complex multi-jurisdictional transactions which account for 29% of the cases notified under the EU FDI Regulation.

- **Inconsistent approach to FDI screening.** There is a perceived inconsistency of what is notified under the EU FDI Regulation, with some Member States suggesting that too many cases are notified, including transactions with no impact on other Member States thus tying up resources. In order to avoid "overloading" the system, suggestions included additional guidelines and the flagging of "more important FDI transactions." Further clarification of key aspects of the EU FDI regulation was also requested, including with respect to trigger dates for notifications and the definition of foreign investor and FDI, among other issues. In addition, there was a suggestion to put in place joint notifications for transactions that qualify for review in more than one Member State.

- **Tight timelines.** The statutory deadlines are too short since they do not give Member States sufficient time to assess complex transactions and ask questions or make comments. This is further complicated by different timelines between Member States' FDI regimes and the EU FDI Regulation.

- **Transparency.** Member States are informed that comments have been provided, but they are unable to view the comments submitted to a notifying Member State by other Member States, nor do they have any visibility as to the content of those comments. In addition, there is no obligation for the notifying Member State to explain how the comments it received have been taken into account (if at all).

In response to the feedback received from Member States, the Commission updated the Frequently Asked Questions to include further details on concepts under the EU FDI Regulation including a definition of FDI and foreign investor; and provided updated versions of the notification form for investors. The Commission also signaled its preparedness to provide additional guidance as required. Moreover, the EU FDI Report recognized that there is scope for further discussion around the interplay between the EU FDI Regulation and other policy instruments and regulators. The Commission is not however prepared to make any changes to the EU FDI Regulation in the short to medium term. It follows that there will be no adjustments to the statutory deadlines or the inclusion of filtering criteria or limiting factors to capture "more important FDI transactions".

As regards multi-jurisdictional FDI notifications, the Commission indicated that coordination across EU Member States warrants careful consideration in the future noting that the issue is not explicitly addressed in the EU FDI Regulation. In doing so, it pointed to multiple challenges, including differing timelines under different national legislation which may prevent synchronization of notifications and assessment under the Regulation. Although the Commission recognizes that there is scope for closer informal coordination, there is a hint of support for joint notifications due to the significant proportion of multi-jurisdictional FDI transactions (29%); and as a means of fully resolving the procedural snags.

Outlook for 2022

It remains the Commission's strong expectation that all 27 EU Member States will put national FDI screening mechanisms in place

As outlined above, there are currently 18 Member States with FDI screening regimes, but an additional five Member States already have consultations or initiatives underway that are expected to result in the adoption of an FDI screening mechanism. The steady increase in Member States with FDI screening regimes along with an expected increase in FDI into the EU will inevitably result in an increase in notifications under the EU FDI Regulation. Investors can therefore expect to find that the coordination of multiple regulatory processes will become even more challenging. In addition to merger control and FDI screening, the draft EU Foreign Subsidies Regulation will add another layer of complexity when it enters into force.

The Commission has launched a comprehensive study to examine variations between the FDI screening regimes of Member States and their policy consequences on the effectiveness and efficiency of the cooperation mechanism in the EU FDI Regulation. The overall objective of the study is to ensure that the Member State FDI screening regimes, as well as the cooperation mechanism, are effective and efficient. This includes the optimization of the interaction between EU Member States' FDI regimes and the cooperation mechanism. There may also be further guidance on the horizon: the Commission indicated that it will consider issuing guidance for the Member State screening authorities and investors noting that they have proven valuable in other policy areas, including anti-trust enforcement.

As the number of Member States with FDI regimes increases, the Commission will have to turn to streamlining its processes to account for the increase in screening activity. The EU FDI Report underscores the importance of ensuring that Commission and Member State resources are utilized in the optimal manner, including sharpening enforcement focus on those FDI transactions that are more likely to pose a risk to security or public order. This will include consideration of how to best handle multi-jurisdictional FDI transactions with the Commission suggesting the possibility of aligning notifications by two or more Member States. The Commission remains cautious and has stressed that it is still early days to consider amending the EU FDI Regulation. It is therefore unlikely that any changes will materialize in the short to medium term. Nevertheless, the EU FDI Report clearly suggests that the Commission is not opposed to the EU adopting a more central role.

France

Key Considerations

- France requires prior authorization if an investor wishes to take control of a "strategic asset". In 2020, the threshold was lowered to 10 percent from 25 percent for listed companies; it remains to be seen whether the threshold will be raised again.
- The Ministry of Finance published its first FDI guidelines in 2022 in order to add much needed clarity to the regime. However the Ministry can depart from its guidelines in specific circumstances, and it confirms a case-by-case approach to several key criteria.
- The Ministry of Finance also published statistics confirming an uptick in enforcement, characterized by the number of undertakings accepted by investors to get clearance of their transaction.

FDI Regime Overview

The French FDI regime requires foreign investors, both from within the European Union (save few exceptions) and abroad, to obtain a prior authorization from the French Ministry of Finance in order to take the control of a "strategic asset" in France. The list of strategic assets is set by decree and is updated periodically. For instance, the list of 20 sectors deemed strategic for the protection of national defense, public order, public authority and public safety – such as weapons, cryptology, energy and water supply, networks and communication – has recently been expanded. It now includes food, news media, and research and development in critical technologies such as cybersecurity, artificial intelligence, semi-conductors, biotechnologies and renewable energies.

Control can be acquired either directly or indirectly, alone or through a shareholder agreement, and the threshold is usually set at 25 percent of voting rights in a company registered in France. However, in July 2020, the threshold was temporarily lowered to 10 percent for public companies. This measure was deemed necessary to protect strategic assets during the pandemic and was initially set to expire at the end of 2020, but it was extended until 31 December 2022 and will most probably remain for at least an additional year.

Procedure

There is an initial review period of 30 business days following the submission of a complete notification. However, the Ministry of Finance may extend this deadline by an additional 45 business days if it intends to request commitments to ensure the protection of national interests. The lowering of the control thresholds has been accompanied by the introduction of a customized review process for investments in public companies. A contemplated investment in a public company must be filed in advance, but may be executed within six months, provided the Ministry of Finance has not raised any objections within 10 business days of the submission of a complete notification.

The French FDI regime lacked transparency but on 8 September 2022, the French Ministry of Economy and Finance issued its first guidelines, intended to make the process more transparent and clear. The Ministry is bound by its guidelines but may nonetheless deviate from them in specific circumstances. The guidelines leave room for discretion on a case-by case approach to key considerations, such as the definition of "strategic sectors" and control, especially in case of joint control. The guidelines also confirm the extensive approach to the definition of a "foreign investor", which can be any type of entity, with or without legal existence, and at any level within the chain of control.

The guidelines clarify that, when investors are expected to undertake certain commitments to get clearance, they are not subject to negotiation. This should be viewed in conjunction with an increase in the number of cases in which commitments have been requested. The types of commitments investors may be required to offer include, among others, maintaining certain assets in France for a given time frame, commitments to supply strategic national clients, protection of national secrets, and governance measures designed to protect public security.

Lastly, the guidelines do not provide transparency on the value of sanctions imposed so far. The amount will depend on the context and the behavior of the investor and can go up to twice the amount of the transaction, 10 percent of the target's turnover or €5 million.

The French Ministry of Finance published its first FDI guidelines in 2022

The Ministry of Finance may oppose an investment only where the commitments offered are unable to address its concerns. However, the most recent reported refusal was brought to the public's attention through the press in 2021: the French Minister for the Economy Bruno le Maire issued a statement that he would use the FDI regime to oppose Canadian Couche Tard investing in the French grocery chain before a filing had even been submitted. The other high-profile prohibition was the decision to block the acquisition of defense supplier Photonis by the U.S. industrial conglomerate Teledyne in 2020. Photonis was then acquired by a French-based PE fund in 2021 at a 30 percent discount. In practice, there have only been a very small number of reported prohibitions. Nevertheless, sellers increasingly seek to shield themselves from the risk of an FDI review by negotiating appropriate protections in the transaction documentation to increase deal security (e.g. completion covenants/undertakings and effort clauses).

Recent months have seen a fine-tuning and rationalization of the FDI legal framework through the publication of the guidelines. It remains to be seen how the French FDI regime will develop, and in particular how it will be balanced against competing policy objectives – on the one hand, there is a desire to remain attractive to non-French investors, and on the other hand, a revived 'dirigiste' industrial policy and desire to create national champions.

Germany

Key Considerations

- Germany remains an investor-friendly jurisdiction, but it has recently tightened its foreign investment rules.
- Investors must notify the German Ministry for Economic Affairs and Climate Protection ("BMWK") before acquiring interests of least 10% or 20% in German entities active in certain business sectors (the relevant threshold depends on the business sector in question).
- The BMWK may initiate a review on its own initiative in the case of an acquisition by a non-EU investor of 25% or more of the voting rights in any German company if the transaction poses a threat to public order or security in Germany.
- The timing of an investment review can be unpredictable, with some complex reviews significantly exceeding the deadlines set out in the applicable laws.

FDI Regime Overview

The German rules on FDI are set out in the German Foreign Trade and Payments Act ("Außenwirtschaftsgesetz"; "AWG") and the German Foreign Trade and Payments Ordinance ("Außenwirtschaftsverordnung"; "AWV"). The BMWK carries out the reviews in consultation with the Foreign Office, the Ministry of Defense and the Ministry of the Interior.

Non-German investors need to notify BMWK before acquiring interests of 10% or more in a German entity that is active in a "sensitive security area" (defense or cryptography sectors). Additionally, investors from outside the EU and the European Free Trade Association (EFTA) must notify the BMWK before acquiring at least 10% or 20% (depending on the relevant business sector) of a German entity that is active in certain other sensitive sectors, including critical infrastructure, certain IT services and IT security products, healthcare and key technologies such as semiconductors and autonomous driving.

The BMWK may initiate a review on its own initiative in case of an acquisition by a non-EU investor of 25% or more of the voting rights in any German company where the transaction poses a threat to public order or security in Germany (so called "cross-sectoral screening"). In order to obtain legal certainty regarding transactions that do not trigger a mandatory notification, non-EU investors often apply for a certificate of non-objection confirming that the BMWK has no objections to the deal.

Timing considerations for transactions

In transactions that trigger mandatory notifications, the BMWK has an initial period of two months to determine whether to open a formal review. If a formal review is opened, it lasts another four months, beginning with the receipt of all relevant documents. The formal review period can be extended by another three months in exceptionally complex cases (four months in defense deals). It can be suspended in case of additional information requests, and for as long as negotiations on mitigation measures are carried out between the BMWK and the parties involved.

In case of (voluntary) applications for a certificate of non-objection, the BMWK must decide within two months whether to issue the certificate or open a formal review. If the two-month period expires without any opening of a formal review procedure, the non-objection certificate is deemed to have been issued.

Recent High-Profile Case

Earlier this year, the planned takeover of German company Siltronic AG by GlobalWafers of Taiwan fell through following a protracted review by the BMWK. Siltronic AG produces silicon wafers, which are an essential resource for the semiconductor industry. The case is noteworthy because the BMWK failed to reach a decision despite a one-year review of the deal.

In late 2020 GlobalWafers made a voluntary public takeover offer to Siltronic's shareholders and filed an application for a certificate of non-objection. The deal collapsed because the BMWK did not conclude its review before GlobalWafers' bid expired on January 31, 2022. In a press release the BMWK stated that "it was not possible to complete all the necessary review steps as part of the investment review" by the end of the period. GlobalWafers and Siltronic are understood to have offered various remedies, including selling security-relevant assets, the possibility to rescind the contract under certain conditions, and/or granting the German government a golden share (i.e., the legal option of Germany to outvote other shareholders under specific circumstances), to no avail.

Another novel aspect of the case is that GlobalWafers sought a preliminary injunction because of the BMWK's inaction requesting that the clearance certificate be deemed to have been issued. However, the courts rejected the company's arguments and ruled in favor of the BMWK.

The key takeaway is that timing of FDI reviews in Germany can be unpredictable in complex cases

The BMWK does not hesitate to make use of its ability to stop the clock where it feels that it needs more time for its review. In practice, review periods may therefore significantly exceed the deadlines set out in the applicable laws.

Outlook for 2022

While Germany remains an investor-friendly jurisdiction, it has recently significantly tightened its rules on non-German investment. In particular, the list of industries considered sensitive has been significantly expanded. Germany's recent FDI reforms are part of a broader series of measures designed to protect German economic interests in what is perceived to be an increasingly hostile global economic climate.

While prohibitions of deals on foreign investment grounds have become more common in recent years, the BMWK has also been inclined to discuss remedies to mitigate security concerns in certain sensitive transactions. All of this means more uncertainty for investors. It remains to be seen whether the BMWK will follow the example of competition authorities and issue practical guidance to help investors better understand the process and the substantive analysis it performs. Irrespective of this, it will be essential for non-German investors considering transactions involving German companies to identify and plan for regulatory challenges posed by Germany's FDI regime at an early stage to avoid unpleasant surprises later on in the process.

Russia

Key Considerations

- Russia's FDI screening regime comprises three mechanisms. One covers 50 sectors of the economy that have been designated as of strategic importance for state defense and security. The second requires review of a transaction of a non-Russian investor with special status, or when certain circumstances are in place. The third mechanism, introduced in response to economic sanctions and export control restrictions imposed on Russia by the US, EU, UK, and other major economies since February 22, 2022, covers certain transactions with non-Russian investors from so-called "unfriendly countries."
- As of the end of 2020, 24 transactions were rejected while just under 300 transactions were approved since the enactment of the first two mechanisms.
- The timing of an FDI review can be uncertain, and reviews can take longer than the statutorily provided 6-month time period. The third mechanism added to the FDI regime is of greater uncertainty in terms of the procedure and the timing of review.

FDI Regime Overview

FDI screening in Russia is based on two main legal instruments: Federal Law No. 57 "On Foreign Investments in Entities Having Strategic Importance for Security and Safety of the State" of April 29, 2008 ("SSL") and Federal Law No.160-FZ "On Foreign Investments" of July 9, 1999 ("FIL") (each as amended), and has recently been supplemented with an additional set of Presidential Decrees adopted after March 1, 2022 (as discussed in the New Restrictions section).

The two main instruments apply to non-Russian investors who plan to acquire an equity interest in or establish control over Russian entities. The regime is overseen by the Federal Antimonopoly Service ("FAS"), which is tasked with the preparatory work, and the Government Commission for Control over Foreign Investments (the "Commission"), which approves such transactions.

The SSL regulates acquisition of control over, or other investments in, Russian companies (or their assets) that are active in 50 sectors of the Russian economy that have been designated as of strategic importance for state defense and security. Those key sectors include: aviation and space activity; cryptography and related equipment and services; mass media and telecommunications (depending on coverage); military equipment and related services; nuclear; survey and mining of natural resources at strategic subsoil plots; and services provided by natural monopolies (e.g., oil and gas pipelines, railroads, ports, and airports). Regulatory clearance is required to acquire "control" over a strategic Russian company. The concept of "control" has been interpreted broadly (as elaborated below).

In contrast to the SSL, the FIL does not specifically cover investments in domestic assets (property) of Russian entities, and it has no sector or industry focus. Instead the FIL requires clearance for (i) investments in Russian entities by foreign states or international organizations (or their affiliates/entities they control) where an equity interest of more than 25% equity interest is acquired, or rights which allow the investor to block decisions/resolutions; and (ii) any investment in Russian entities where the Head of the Commission who is the Chairman of the Russian Government has requested a review (so called "ad hoc cases"). These reviews are rarely triggered and typically arise where a particular transaction does not fall under any of the 50 strategic sectors covered by the SSL (e.g., an acquisition of a major coal mine or critical supplier to the government). The FIL may also apply to acquisition of equity interests through the establishment of a Russian entity (where the SSL does not apply). Post-completion notifications need to be submitted to the FAS including following the completion of a transaction where the Commission issued its prior approval or following acquisition of 5% or more equity interest in a strategic entity.

The Commission has broad powers and may require non-Russian investors to enter into written commitments as a condition of approval. A transaction clearance granted to a non-Russian investor must set out the timing for the closing to occur. A failure to seek approval for a notifiable transaction would render it void and lead to related consequences (e.g., restitution, loss of voting rights on application to a Russian court).

Timing considerations for transactions

Under the SSL, the Commission should issue its decision within a maximum review period of six months. Nevertheless, the statutory deadline is not always respected. Although decisions may be issued within the initial review period of three months, the timing is uncertain since (i) the Commission is an *ad hoc* body which does not hold regular meetings (e.g., reports indicate that only one and two meetings took place in 2020 and 2021, respectively), and (ii) the review process requires the input of multiple Government departments (e.g., the Ministry of Defense, the Federal Security Service), which is often delayed. The SSL contains a simplified clearance procedure, but only a limited number of transactions may benefit from it, e.g., if a company generally operates in non-strategic areas, but has certain listed strategic assets.

The FIL does not establish a bespoke review process for notifiable transactions; rather, the law provides that the procedures of the SSL apply. However, the authorities have a broad margin of discretion as regards the interpretation and application of the statutory deadlines for FIL approval under the procedures set out in the SSL. Therefore, although the time limit of six months applies, it often takes longer in practice. In addition, there is no statutory deadline for the Head of the Commission to make a decision as to whether a transaction should be reviewed as an ad hoc case and delays of several months are not uncommon.

Non-Russian investors should also reserve at least one additional month to prepare the filing given a need to obtain notarized and apostilled documents and prepare their Russian translations (and in certain cases to disclose ultimate beneficial owners in advance).

Recent enforcement practice

Russian authorities only sporadically disclose statistics on filings under the FIL and SSL. Nevertheless, according to publicly available figures, the vast majority of transactions are approved. As of the end of 2020, 24 transactions were rejected and just under 300 transactions were approved since the enactment of FIL and SSL. In addition, a high number of applications were not considered by the Commission in the first place since the FAS found that no clearance was in fact required, or the parties withdrew their application.

Only a small number of court cases have been initiated under the FDI regime established by the SSL and FIL. In one recent notable case, the Constitutional Court of Russia upheld the position of FAS and Russian state arbitrazh (commercial) courts that authorities enjoy broad discretion in determining whether an entity is considered strategic under SSL. The appeal to the Constitutional Court arose from Canrig Drilling Technology Canada Ltd. unsuccessfully challenging the FAS' position in the lower courts that providing technical servicing for drilling equipment at a subsoil plot of federal importance by a *Russian* company constituted a strategic activity. Canrig Drilling Technology Canada Ltd.'s claim centered on the fact that the services it provided were not specifically listed in the SSL as a "strategic" activity and was therefore incorrectly categorized by the FAS as the "geological survey of subsoil plot and extraction of minerals at deposits having federal significance."

In another ongoing case (A55-6479/2020), the FAS imposed a series of interim measures on Elliott Group ("Elliott") and other companies involved, including the suspension of its voting in connection with their acquisition of indirect control of the Russian subsidiaries of Arconic Inc ("Arconic"), JSC "Arconic SMZ" and JSC Alti Forge. The Russian subsidiaries are active in the manufacturing and sales of metals used in combat equipment and thus deemed to be active in a sector of strategic importance. The FAS considered that Elliott exercised indirect control since, *inter alia*, it had the power to nominate a number of its representatives to the Board of Directors of Arconic.

The FAS rejected Arconic's claim that Elliott did not control Arconic since the Board members nominated by Elliott are independent directors under U.S. laws. The case is still ongoing in Russian state Arbitrazh (commercial) courts.

New Restrictions

In response to economic sanctions and export control restrictions imposed on Russia by the U.S., EU, UK and other major economies since February 22, 2022, the FDI regime has changed dramatically, and it is unclear how long such changes will last. The Decree of the Russian President, dated March 1, 2022, provides, among other things, that the following transactions are only permitted subject to prior approval by the Commission:

- providing loans to "foreign persons of unfriendly countries"; and
- any transactions with "foreign persons of unfriendly countries" which would give rise to a property right to securities and real estate. As currently construed, this essentially restricts transfers of title to securities of Russian companies and real estate to or by affected non-Russian persons; however, the scope of this restriction could potentially be construed more widely so as to apply to the transfer of any equity interest, or to indirect transfers. Therefore, practically, we would advise filing for clearance even in scenarios where this is not evidently required.

These restrictions do not apply to transactions involving the Russian Central Bank or any organ of the Russian state authority as a party. The list of "unfriendly countries" currently includes all major countries that have imposed sanctions against Russia (including the United States, Australia, the UK including overseas territories, and the EU). The restrictions outlined above would apply to all citizens of "unfriendly countries" including individuals, entities with a principal place of business or who are registered in such countries, and those whose income is principally derived or generated from such countries.

A number of other statutory acts were adopted during March – May 2022; these acts provide further details, including potential exemptions from the restrictions outlined above, and set out additional limitations.

Outlook for 2022

It is difficult to predict how the situation in Russia will unfold in the near term, including which new restrictive measures may be further put in place by US, EU, UK and other countries, as well as any counter-sanctions by the Russian Government.

Regardless of this situation, there have been continuous refinements to the Russian FDI regime, and this trend is expected to continue. This has included further amendments to the existing

regime and decisional practice from the courts on the interpretation of existing provisions. Most recently, a number of bills were introduced for public discussion (prior to their consideration by the Russian Parliament), which propose, among other things, (i) additional recourse for failure to obtain transaction clearance (e.g., the seizure of acquired shares by the state), (ii) clarification of scope of jurisdiction/notifiable transactions (e.g., if a Russian individual who already has control over a strategic entity obtains foreign citizenship), (iii) clarifying and expanding the list of strategic activities (e.g., inclusion of fishing). In addition, a recent 2022 bill focused on de-offshorization proposes a simplified procedure for obtaining clearance of transactions under SSL for certain international organizations which have re-domiciled to Russian special administrative zones.

Another recent trend, which has shown no signs of abating, has been the FAS' increasingly expansive approach to jurisdiction. In particular, the FAS has taken a broad view of the concept of "control." In several cases, the FAS has found that "control" includes the ability to veto or block resolutions of a target (i.e., negative control) in addition to the acquisition of a majority stake, or ability to adopt major corporate decisions of the target. In addition, the FAS' assessment of control will take into account a wide range of factors/links including professional and family connections. The FAS' increased assertiveness coupled with its broad interpretation of the concept of control increases regulatory uncertainty and will lead to a corresponding increase the number of transactions that are potentially caught by the SSL and FIL.

Following changes in the composition of the Commission and appointment of a new head of the FAS in 2020, the FAS reportedly offers non-Russian investors fewer opportunities to engage and discuss their applications. The delays for the consideration of applications have also increased. Non-Russian investors may expect that similar complications will persist in 2022 and beyond.

United Kingdom

Key Considerations

- A new FDI screening regime entered into force on January 4, 2022. The rules apply retroactively to investments made since November 12, 2020.
- The newly created Investment Security Unit (ISU) will oversee enforcement.
- The regime foresees broad and extensive powers to intervene in investments and will involve mandatory suspensory notifications of transactions involving qualifying entities in sensitive sectors.

FDI Regime Overview

The National Security and Investment Act 2021 ("NSIA") was passed on April 29, 2021, and came into force on January 4, 2022, ushering in the UK's first comprehensive FDI screening regime. "Foreign" is a misnomer, though, since the new regime does not distinguish by nationality of investor. The NSIA gives the UK Government wide-ranging standalone powers to review and intervene in transactions on national security grounds. This includes a mandatory notification regime for transactions in 17 designated sensitive areas of the UK economy.

Post-Brexit, the UK Government has been keen to stress that the country remains open for business

and that it only expects a small proportion of the transactions it reviews will qualify for a full-blown national security assessment.

Early experience of the regime in operation reflects favorably on the new procedures. Nevertheless, the regime's sweeping powers and long jurisdictional reach, as well as its retrospective application, add to an increasingly complex regulatory landscape for transactions.

The NSIA casts the net wide and captures investments involving (i) qualifying entities, which carry out activities or supply goods or services in the UK, and (ii) qualifying assets, which are used in connection with activities or the supply of goods or services to people in the UK. Qualifying entities captures a broad range of legal structures, including companies, limited liability partnerships, any corporate body, trusts and unincorporated associations. Qualifying assets includes tangible property such as land and moveable objects as well as intangible property such as intellectual property.

Unlike the UK merger control regime, the NSIA has a much broader jurisdictional scope since its criteria are not framed by reference to minimum turnover or share of supply thresholds. Instead, investments that trip the following control thresholds in the defined sensitive areas of the economy fall within the scope of the Act ("qualifying acquisitions"), irrespective of the nationality of the investor:

- shareholding or voting rights in a qualifying entity exceed 25%, 50% or 75% (the NSIA also captures increases in shareholdings/voting rights above the thresholds);
- ability to pass or block resolutions governing affairs of a qualifying entity;
- ability to materially influence policy of a qualifying entity;
- ability to use a qualifying asset, or direct or control its use, or the ability to do so to a greater extent than prior to the acquisition. The indirect acquisition of rights may also need to be notified.

The 17 sensitive areas of the economy include: advanced materials; advanced robotics; artificial intelligence; civil nuclear; communications; computing hardware; critical suppliers to government; cryptographic authentication; data infrastructure; defense; energy; military and dual-use items; quantum technologies; satellite and space technologies; synthetic biology; and transport.

Although the Government has indicated that it intends to focus on UK-based entities and assets, the NSIA has extraterritorial reach since it applies to any entity or asset that is connected to the UK through activities carried on in the country or the supply of goods or services to local customers. The connecting factors which may be taken into account in determining whether an overseas entity falls within the scope of the Act include, but are not limited to, local presence such as an office or branch; the supply of goods that are modified or used domestically; and carrying out R&D activities in the UK. Investigations of overseas asset acquisitions are expected to be even rarer, but the Act could apply to assets that are used in connection with the supply of goods or services to the UK or the generation of energy or materials consumed domestically.

Mandatory versus voluntary notification

The mandatory regime applies where the shareholder or voting rights acquired by the acquirer in a qualifying entity which is active in the relevant sectors exceed 25%, 50% or 75%; or confer the ability to pass or block resolutions governing its affairs ("notifiable acquisitions"). A failure to seek approval for a notifiable acquisition before completion will render it void. In addition, the acquirer may be subject to criminal or civil penalties for completing the transaction without obtaining clearance. Acquisitions of assets are exempt from the mandatory notification obligation, although the Government may

choose to exercise its call-in power where it identifies a potential national security risk.

For qualifying acquisitions falling outside the mandatory regime – including the acquisition of material influence and qualifying assets – the assessment of whether the Government should exercise its call-in power is based on three risk factors:

- **Target risk.** If the target of the qualifying acquisition (the entity or asset being acquired) is being used, or could be used, in a way that raises a risk to national security. This assessment may also take into consideration of potential risks arising from the target's proximity to sensitive sites.
- **Acquirer risk.** Whether the acquirer has characteristics that suggest there is, or may be, a risk to national security from the acquirer having control of the target. The judgement will not be based solely on an acquirer's country of origin, but ties or allegiance to a state or organization which is hostile to the UK will be considered in the assessment of whether there is a national security risk.
- **Control risk.** The amount of control that has been, or will be, acquired through the qualifying acquisition. A higher level of control may increase the level of national security risk.

The call-in power is broadly framed, and the Government is able to retrospectively review transactions that closed on or after November 12, 2020, for a period of up to five years (or up to six months after becoming aware of the transaction). Parties to transactions that are not caught by the mandatory regime are able to submit voluntary notifications to get certainty that the Government does not intend to exercise its call-in power. In addition, it is possible to submit retrospective validation applications for completed transactions.

Process

The NSIA regime is overseen by the Investment Security Unit ("ISU"), which sits within the Department of Business, Energy and Industrial Strategy ("BEIS"). The assessment of qualifying acquisitions is divided into two parts: a "review period" of 30 working days following the submission of a complete notification; and an assessment period of 45 working days if an acquisition is called in for a full national security assessment. Where a notification is rejected, the ISU will inform the parties of the reasons it was not accepted. According to UK Government estimates, 80-90% of acquisitions are expected to be cleared within the initial review period.

The ISU has broad investigatory powers including the ability to request information and meetings with the parties. The NSIA also foresees a wide range of remedies to address national security concerns. This includes the power to block transactions, to impose conditions as an element of clearance, and to issue interim orders to prevent parties from taking action which may undermine the ISU's ability to effectively resolve potential national security concerns.

Outlook for 2022

At a time of increased protectionist sentiment and increased geo-political tensions, the enactment of the NSIA is part of a wider trend of an ever-increasing number of jurisdictions adopting FDI regimes. The Government has been at pains to underline that it intends to take a "risk-based, proportionate and consistent" approach and that will seek to "minimize burdens on business throughout." It remains to be seen whether this is borne out in practice, but the early signs have been encouraging in terms of the ISU's responsiveness and willingness to engage with parties. Moreover, the ISU has made efforts to coordinate its review process with other UK regulators, notably the Competition and Markets Authority.

Although the Government expects that the vast majority of acquisitions will be cleared within the initial review period, the regime's low thresholds will impact the transaction timeline of non-problematic deals. This is to some extent alleviated by the strict statutory deadline of 30 working days for the initial review period which may ease transaction planning for deals where potential security concerns are unlikely to be identified.

United States

Key Considerations

- The Committee on Foreign Investment in the United States ("CFIUS" or the "Committee") is an interagency committee that has broad powers to review foreign investments in and acquisitions of U.S. businesses to determine the potential impact on U.S. national security.
- Increased dealmaking and a recent expansion in the Committee's jurisdiction demand greater attention from transaction parties to potential CFIUS considerations from the beginning of the transaction process to identify risks and manage potential impediments to closing.
- In particular, transaction parties should evaluate CFIUS considerations around investments in U.S. businesses that involve critical technology, critical infrastructure, and sensitive personal data.
- Investors should conduct due diligence to understand national security touchpoints on all sides of a transaction. A sophisticated CFIUS strategy that accounts for an investor's objectives and anticipates and mitigates potential U.S. national security risks increases the likelihood that transaction parties will reach closing on their preferred timing.

FDI Regime Overview

The Committee has the authority to approve transactions, impose mitigation measures, suspend transactions and, where appropriate, recommend that the President block or unwind transactions. Recently, key areas of concern for CFIUS have included the semiconductor industry and entities that handle Americans' sensitive personal data, including financial services companies, healthcare service providers and even dating apps (see our OnPoint). Parties can prepare for CFIUS scrutiny by conducting due diligence and structuring deals with national security concerns in mind.

The Committee's jurisdiction encompasses:

- Mergers, acquisitions, and takeovers that could result in a non-U.S. person acquiring control over a U.S. business;
- Certain non-controlling investments by non-U.S. persons in U.S. businesses associated with critical technology, critical infrastructure and sensitive personal data (with mandatory filing requirements for transactions involving certain U.S. businesses dealing in critical technologies or non-U.S. persons affiliated with non-U.S. governments, including sovereign wealth funds); and
- Transactions involving the purchase or lease by, or concession to, a non-U.S. person of certain U.S. real estate that might raise national security concerns.

Transactions are brought to the Committee's attention through filings that take the form of either "notices" or "declarations." It generally takes a few weeks to a month to prepare a filing, though this timing can be accelerated. Notices are multi-page, in-depth descriptions of the transaction and parties that result in a four- to six-month review process and possible investigation. Notices can result in the deal being cleared to proceed; being subject to mitigation measures to protect national security concerns; or, in rare cases, being blocked. Declarations, by contrast, are typically no longer than five pages and present a simplified method of informing CFIUS of a transaction. Following submission,

CFIUS has 30 days to review a declaration. The Committee may respond to a declaration in one of four ways, by informing parties that it: has cleared the transaction; is initiating a unilateral review; is requesting that the parties submit a full formal notice; or is unable to reach a decision regarding clearance based on the declaration alone

The possibility of an uncertain conclusion to the review of a declaration often leads party to elect to file a full notice from the start.

Recent enforcement practice

In July 2021, CFIUS published its latest Annual Report to Congress on key activities, including notices, declarations, and withdrawals through 2020 ("Annual Report"). The Annual Report reflected an ongoing trend in high numbers of filings; there were 313 total filings in 2020—up approximately 300% from 2010. Japan led the number of notices filed (19), followed by China (17), while Canada led the number of declarations filed (20) followed by Japan (18).

We expect that 2021 has continued the trend in high filing numbers, given the uptick in dealmaking in the past year

The high volume of deals in the past year together with the Committee's expanded jurisdiction as a result of the Foreign Investment Risk Review Modernization Act ("FIRRMA") has demanded greater attention from transaction parties to potential CFIUS considerations from the very start of the transaction process to identify risks and manage potential impediments to closing. There is particular scrutiny around certain investments involving critical technology, critical infrastructure, and sensitive personal data, especially when such transactions involve Chinese investors.

The Committee's focus on critical technologies has been made clear through intense scrutiny around investments in the global semiconductor industry. In December 2021, South Korean semiconductor chip maker Magnachip Semiconductor Corp. ("Magnachip") and Wise Road Capital ("Wise Road"), a Chinese private equity firm, mutually agreed to terminate a USD 1.4 billion transaction. Magnachip and Wise Road did not submit a CFIUS filing at the time the transaction was announced in March 2021. The parties reportedly believed that the transaction was outside the Committee's jurisdiction because Magnachip conducted its manufacturing, research and development, and sales activities outside the United States. Its only U.S. ties were its public listing on the New York Stock Exchange and a Delaware-organized entity that owned other entities that conduct business outside the United States. However, CFIUS determined that it had jurisdiction over the transaction. The parties subsequently received and complied with a request from the Committee to submit a filing, but ultimately were unable to obtain CFIUS approval. Magnachip's August 2021 SEC filing indicated that the Committee was unable to identify "any mitigation measures … that would adequately mitigate the identified risks." The Magnachip transaction is notable because it demonstrates the breadth of the Committee's view of its jurisdiction and the heightened level of concern regarding Chinese investments in sensitive industries. CFIUS can impact transactions where the U.S. component of a business is a limited part of a non-U.S. company's operations.

Investment from China may be subject to particular scrutiny, but assessing structures and methods for allaying potential national security concerns can go a long way towards ensuring that a deal is cleared by CFIUS. For example, in 2021 CFIUS cleared a transaction involving a Chinese investment company, Genimous Investment Co., Ltd., which had acquired a U.S. data-driven marketing company, Spigot, in 2016. The parties had not made a CFIUS filing in 2016, but again CFIUS invited parties to submit a filing. Once the Committee completed its review of the transaction, it required the parties to sign a national security agreement and imposed several mitigation measures, including requiring that a majority of the boards of Spigot and its immediate parent companies comprise CFIUS-approved U.S. citizens and that Spigot not transfer any U.S. persons' data outside the United States without prior approval. The timing of the clearance, five years after the transaction, serves as a reminder of the long reach of CFIUS jurisdiction. Still, the clearance offers hope for Chinese investors interested in investing in or acquiring U.S. data companies, especially where potential investors can propose and implement mitigation measures.

Outlook for 2022

In 2022, we expect to see more deals and more scrutiny—for some investors. Dealmaking activity shows no signs of slowing down, but the number of Chinese investments in the United States has been on the decline over the past few years, likely due to the greater attention CFIUS pays to Chinese investors. At the same time, investors from Australia, Canada, New Zealand, and the UK—CFIUS "excepted foreign states"—may have an advantage over other non-U.S. investors when it comes to investment opportunities, as companies seeking investors (and sellers comparing competing buyers) consider the potential CFIUS complications of each potential transaction partner.

When contemplating a transaction, investors should conduct due diligence to understand national security touchpoints on all sides of a transaction, including the investors and the investment target. Whether the target business is a contractor for the U.S. Government, and whether it is involved in critical technology, critical infrastructure, or sensitive data should all be considered. A sophisticated CFIUS strategy that accounts for an investor's objectives and mitigates potential national security risks can make a significant difference.

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