

Riding the New FDI Regulation Wave



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Tightening Foreign Direct Investment (FDI) screening systems has become a global trend in the last few years (see also our M&A Series of October 2017). Its focus has always been mainly national security concerns, but Covid-19 seems to have accelerated and intensified this trend. FDI is also used now to protect broader economic and social concerns in environments disrupted by Covid-19.

The EU, which is the epicenter of the pandemic and also the main destination for FDI across the globe, has taken a step towards foreign investment by adopting the FDI Regulation. This signifies its departure from its historically more relaxed attitude, prompting a majority of the Member States to rapidly follow suit by tightening their existing FDI systems or adopting new ones.

This new regulatory environment adds another layer of complexity to deal making and urges players to prepare properly and thoroughly to improve their deal success.

Measuring the Wave - EU Cooperation Framework and Rapid Growth of Far-reaching National Regimes

The FDI Regulation (Regulation No. 2019/452) aims to coordinate the screening of FDI that has an EU dimension and that could impact security or public order. In pursuit of this, Member States must therefore exchange information between each other and with the EU Commission. The EU Commission can—and must in some circumstances—issue a non-binding opinion on the FDI, and EU Member States may react to an investment that is under review by another Member State. Yet, the final decision remains with the relevant Member State. The EU Commission will also be able to intervene in a deal up to 15 months following completion if it concerns transactions that are completed but have not been screened. This rule applies retroactively to deals completed after 10 July 2019.

Member States had until last month (11 October 2020, to be exact) to implement the cooperation

mechanism under the FDI Regulation. Although all Members States must comply with the cooperation mechanism, there is no obligation for them to adopt their own screening mechanism. To date, only 15 Members States have screening mechanisms in place, 6 have pending screenings, and 5 do not even have any at this time. The UK will also become a foreign investor in the EU shortly.

Belgium currently has a limited FDI-regulating system for the Flemish public sector only, while there is also a draft federal bill, it is in a preliminary phase with no official draft being available yet. It remains to be seen to what extent Belgium will follow and be inspired by the FDI screening regimes already in place in its neighboring countries. Some of them, e.g., France, the Netherlands, Germany, Spain, and Italy, have indeed introduced or revised their FDI screening mechanisms recently. The breadth of some of the rules indicate that they could impact a significant range of investments: acquisitions of minority interests and non-controlling interests, special voting rights, assets, and IP, etc. Key industry sectors often go beyond the traditional national security sectors, and the test will be to define these sectors. Finally, some FDI systems will even apply retroactively, just like those already being implemented in the Netherlands and the UK.

Surfing Tricks & Manoeuvres - Assessing, Negotiating and Allocating the Regulatory Risk

The new regulatory environment clearly adds another angle for manoeuvring the deal complexity, as it increases deal uncertainty. First of all, parties should assess the risk of a post-completion application of the cooperation mechanism for completed transactions that have not been screened from July 2019 onwards. A similar risk assessment needs to be made for transactions that are subject to relevant national FDI systems that apply retroactively.

For any ongoing and future relevant transactions, parties need to keep themselves informed about the fast-changing regulatory landscape and to perform an upfront regulatory risk assessment far beyond the traditional security and defence sectors. Planning ahead for potential EU and national intervention at an early stage is crucial. This requires sufficient access to the information on the target. The information will enable you to establish whether the transaction falls within the scope of a relevant FDI regime. Parties will also need to identify a regulatory strategy and agree on how to engage with the relevant regulators. All of the foregoing will impact the deal documentation, including conditions precedent and cooperation provisions, among others.

Given that non-compliant transactions are at risk of being fined, conditioned, prohibited or even unwound, parties will strive to complete riding this wave successfully.