Baker McKenzie.

2017

RISING SCRUTINY

Assessing the global foreign investment review landscape

A BAKER MCKENZIE REPORT

November 2017

CONTENTS

Executive summary 4

Introduction 10

Factors driving greater scrutiny 16

Strategies to close the deal 24

Regulatory updates 32

- Australia 34
- Canada 38
- United States 42
- European Union 48
- France 52
- Germany 56
- Italy 60
- Spain 62
- United Kingdom 64

EXECUTIVE SUMMARY

- Six of the eight most advanced economies surveyed in this report have changed their foreign investment review procedures since 2014 (Australia, Canada, France and Germany) or are considering doing so (the United Kingdom and the United States). The EU has also put forth a proposal to establish a new EU framework for screening foreign investment.

- Advanced economies are rethinking their approaches to foreign investment policy, primarily due to record levels of Chinese investment, increased activity by state-owned enterprises and sovereign entities and changing ideas about national and economic security.

- These changes are impacting the M&A landscape. In 2016, for example, the number of canceled China outbound transactions jumped to a record 30 deals worth $74 billion (10 deals worth USD 59 billion in the US and 20 deals worth $16.3 billion in Europe). By comparison, 23 transactions worth $7.9 billion were canceled in 2015 and 13 deals worth USD 2 billion were canceled in 2014. Greater regulatory and political scrutiny in North America and Europe contributed to the increase.

- While China features prominently in the headlines, the regulatory fallout is much broader. Policy changes will impact investors from around the world, including SOEs from major emerging markets, buyers from sensitive regions and countries such as the Middle East and Russia, as well as purchasers from all regions focused on sensitive technologies. These developments should be viewed as indicative of shifting market sentiment. All investors, regardless of their country of origin, need to proactively manage stakeholder interests as part of their deal strategy.

- The most scrutinized industries worldwide include: Defense, Critical Infrastructure, Information Technology, Telecommunications, Energy, Natural Resources, and Agriculture.

- With the Committee on Foreign Investment in the United States (CFIUS) reportedly on track to review more than 250 transactions in 2017, foreign investors are paying keen attention to developments in the US (particularly in light of the number of European companies with US operations and evidence of increasing coordination among authorities). Recent data presented by CFIUS highlight an increase in the volume and complexity of reviews and the emergence of Chinese acquirers as the top investors before CFIUS. These trends are likely to continue.

- Despite more scrutiny of transactions in many advanced economies, the vast majority of deals continue to be approved.

    - In 2015, the most recent year for which there is data, CFIUS imposed mitigation measures on 8% of the covered transactions it reviewed (11 of 143), a similar figure to the 6% of covered transactions that cleared with mitigation measures (9 of 147) in 2014.

    - The Australian government considered 43,013 foreign investment applications in 2015-16, up from 13,322 in 2012-13. Only five deals were rejected.

    - In fiscal year 2016-17, the Canadian government reviewed 22 applications and 715 notifications for potential national security concerns and conducted 5 formal national security reviews. In 3 cases, the non-Canadian was ordered to divest itself of control of the Canadian business; in 2 cases, the investment was authorized with conditions.

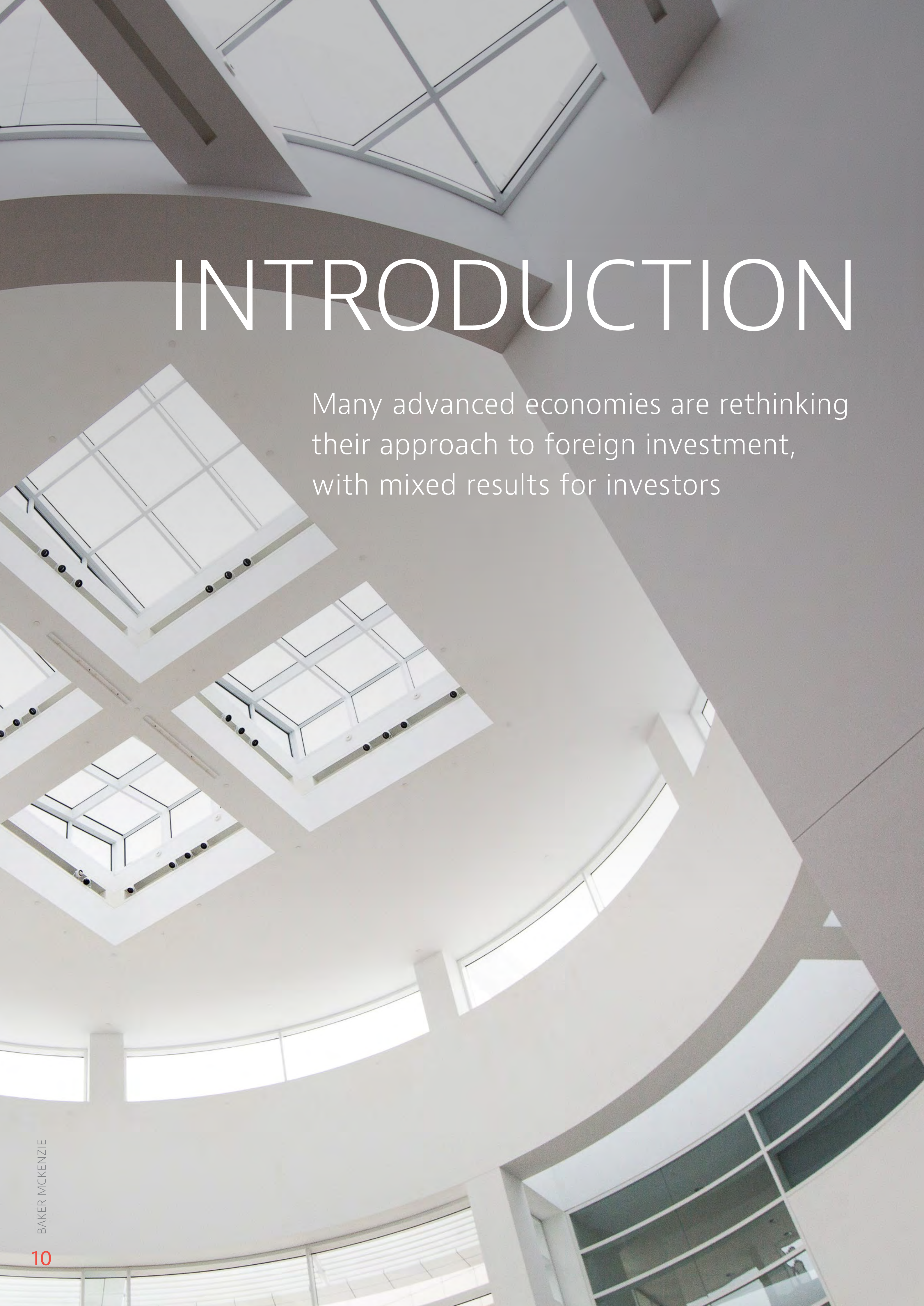
- While most cross-border transactions still have a high likelihood of being approved – and foreign investors may even benefit from more streamlined review processes – those in sensitive sectors (e.g., advanced technologies, telecommunications, infrastructure, natural resources) may encounter more scrutiny and face a prolonged approval process.

In 2016, the number of canceled China outbound transactions jumped to a record 30 deals worth $74 billion (10 deals worth $59 billion in the US and 20 deals worth $16.3 billion in Europe).

—

Strategies for foreign investors

- Conduct an early risk assessment
- Elevate national security risks for investors with any hint of a state affiliation
- Take a global view of national security risks
- Craft a public and government relations strategy
- Engage with the reviewing body early
- Understand the process and timeline
- Be prepared to make detailed disclosures
- Consider deal terms to allocate risk and responsibility
- Consider mitigation measures as part of transaction strategy
- Don't forget about other regulatory hurdles



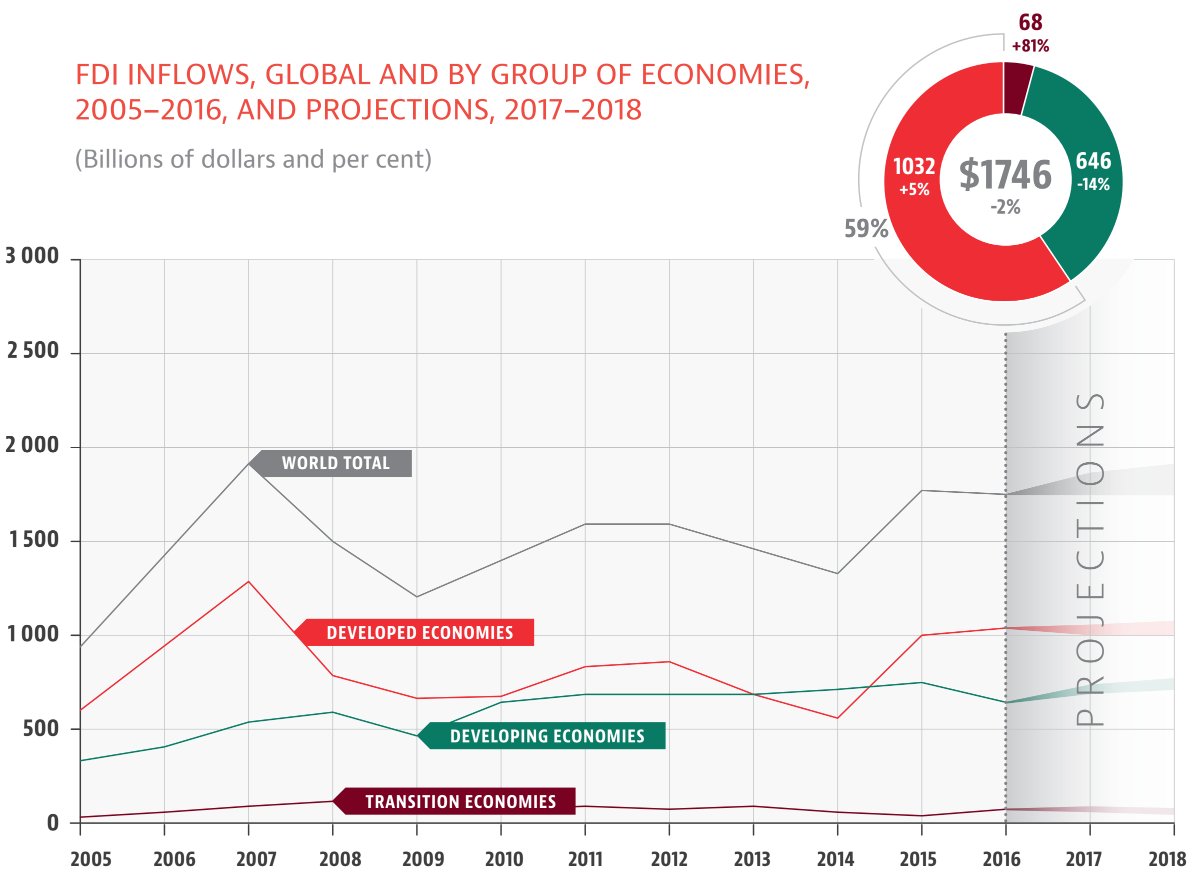
INTRODUCTION

Many advanced economies are rethinking their approach to foreign investment, with mixed results for investors

Most advanced economies have long adhered to an open, rules-based approach to foreign investment, and have benefitted both as large global investors and as recipients of foreign investment. While global flows of foreign direct investment (FDI) fell slightly in 2016, flows to developed economies increased by 5% to USD 1 trillion, according to the 2017 United Nations World Investment Report.[1]

FDI INFLOWS, GLOBAL AND BY GROUP OF ECONOMIES, 2005–2016, AND PROJECTIONS, 2017–2018

(Billions of dollars and per cent)



Source: ©UNCTAD, FDI/MINE database (www.unctad.org/fdistatistics)

[1] United Nations Conference on Trade and Development, World Investment Report: Investment and the Digital Economy (New York: United Nations 2017)

DEVELOPED ECONOMIES
FDI Flows, 2016

(Value and change)

Source: United Nations Conference on Trade and Development, World Investment Report: Investment and the Digital Economy (New York: United Nations 2017).

In view of risks to global growth, many advanced economies have reaffirmed their openness to foreign investment to promote jobs, innovation and economic growth. In the last year, countries such as Australia, Canada and Germany have clarified their foreign investment review frameworks to increase the transparency of the process and provide more certainty to investors.

COUNTRY	NEW REGULATIONS SINCE 2016	MAIN FDI LAWS*	REVIEWING BODY
Australia	Yes	Foreign Acquisitions and Takeovers Act of 1975; Foreign Acquisition and Takeovers Regulation 2015	Foreign Investment Review Board under the Ministry of Treasury
Canada	Yes	Investment Canada Act	Investment Review Division of Innovation, Science and Economic Development Canada; Department of Canadian Heritage
France	No	Article R153-1 and seq. of the French Financial and Monetary Code, expanded by the Montbourg Decree Dated 14 May 2014	Ministry of Economy, with possible inclusion of other ministries
Germany	Yes	Foreign Trade and Payments Act of 2004	Ministry for Economic Affairs and Energy
Italy	No	Law no 56 dated 11 May 2012, Presidential Decree No 35 dated 19 February 2014.	Office of the Prime Minister
Spain	No	Law 18/1992 of July 1	Varies based on the sector of the target company, type of investment and/or nationality of the investor
United Kingdom	No	No specific regulation of foreign investors	N/A; Competition and Markets Authority is responsible for merger control
United States	No	Exon-Florio Amendment to the Defense Production Act of 1950, as amended by the Foreign Investment and National Security Act of 2007 (FINSA)	CFIUS

* Other laws and regulations may apply to acquisitions and investments by foreign investors, including in certain industries.

Yet the investment policy landscape is becoming more complex as nations respond to the effects of globalization, cybersecurity threats, state development strategies and geopolitical risks. While advanced economies remain eager to attract FDI, many have enacted – or are considering – new legislation to broaden the scope of government review of cross-border investments to address national security concerns.

In this report, we examine the shifting foreign investment review landscape in select advanced economies, focusing on eight of the world's key FDI jurisdictions – Australia, Canada, the US, France, Italy, Germany, Spain and the UK - and the EU. In the last few years, some of the most influential economies have reformed their foreign investment review frameworks to allow the government more leeway to block deals or impose conditions on their completion.

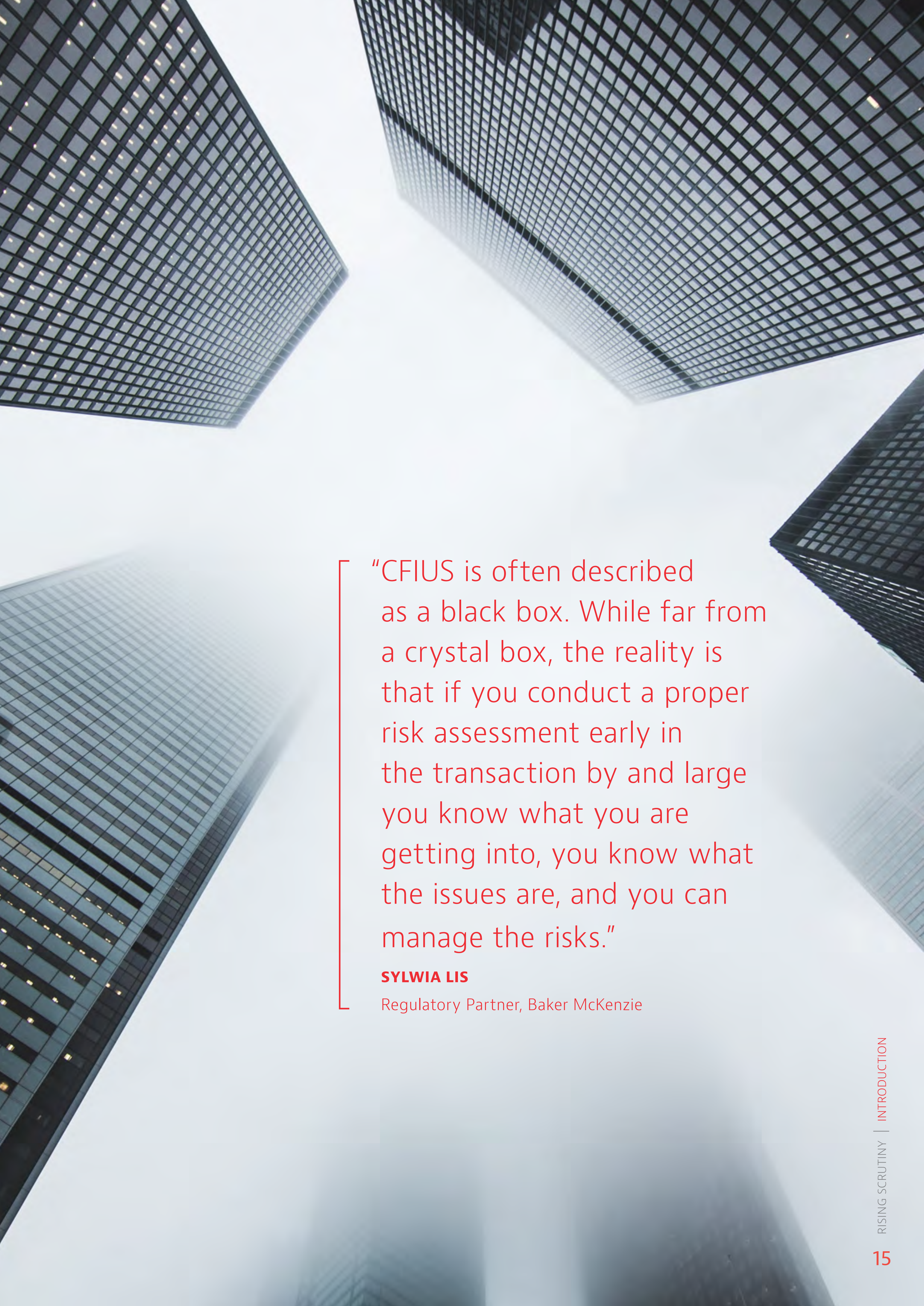
Other countries are ramping up scrutiny of investments in sensitive sectors to address national security risks. And independent of changes to host country laws, foreign governments are increasingly coordinating with each other where transactions involve assets in multiple jurisdictions. In February 2017, for example, the leaders of Italy, Germany and France proposed that the EU Commission investigate more closely when foreign investment targets strategic sectors across the Union (although other EU countries took a diametrically opposed position).

The upshot is that while most cross-border transactions still have a high likelihood of being approved – and many foreign investors are benefitting from more streamlined review processes – those in sensitive sectors such as advanced technologies, telecommunications, infrastructure and natural resources may now encounter more scrutiny and face a prolonged approval process.

"Germany has a very high threshold in terms of state intervention in transactions," says Thomas Gilles, an M&A partner in Baker McKenzie's Frankfurt office. "We are not aware of a single transaction, with the exception of a few with a CFIUS component, prohibited by the German Ministry for Economic Affairs and Energy. Yet the seller may make a business judgment that it will be more difficult to bring a transaction to conclusion with a buyer that triggers concern under foreign investment review laws in Germany or other relevant jurisdictions."

Based on heightened concerns in advanced economies across the world – and the sense that more change is coming – sophisticated foreign investors are working through these issues with their advisors right away. In this report, we identify the strategies that foreign investors will need to deploy to get their deals approved. "CFIUS is often described as a black box," says Sylwia Lis, a regulatory partner in Baker McKenzie's Washington, DC office. "While far from a crystal box, the reality is that if you conduct a proper risk assessment early in the transaction by and large you know what you are getting into, you know what the issues are, and you can manage the risks."

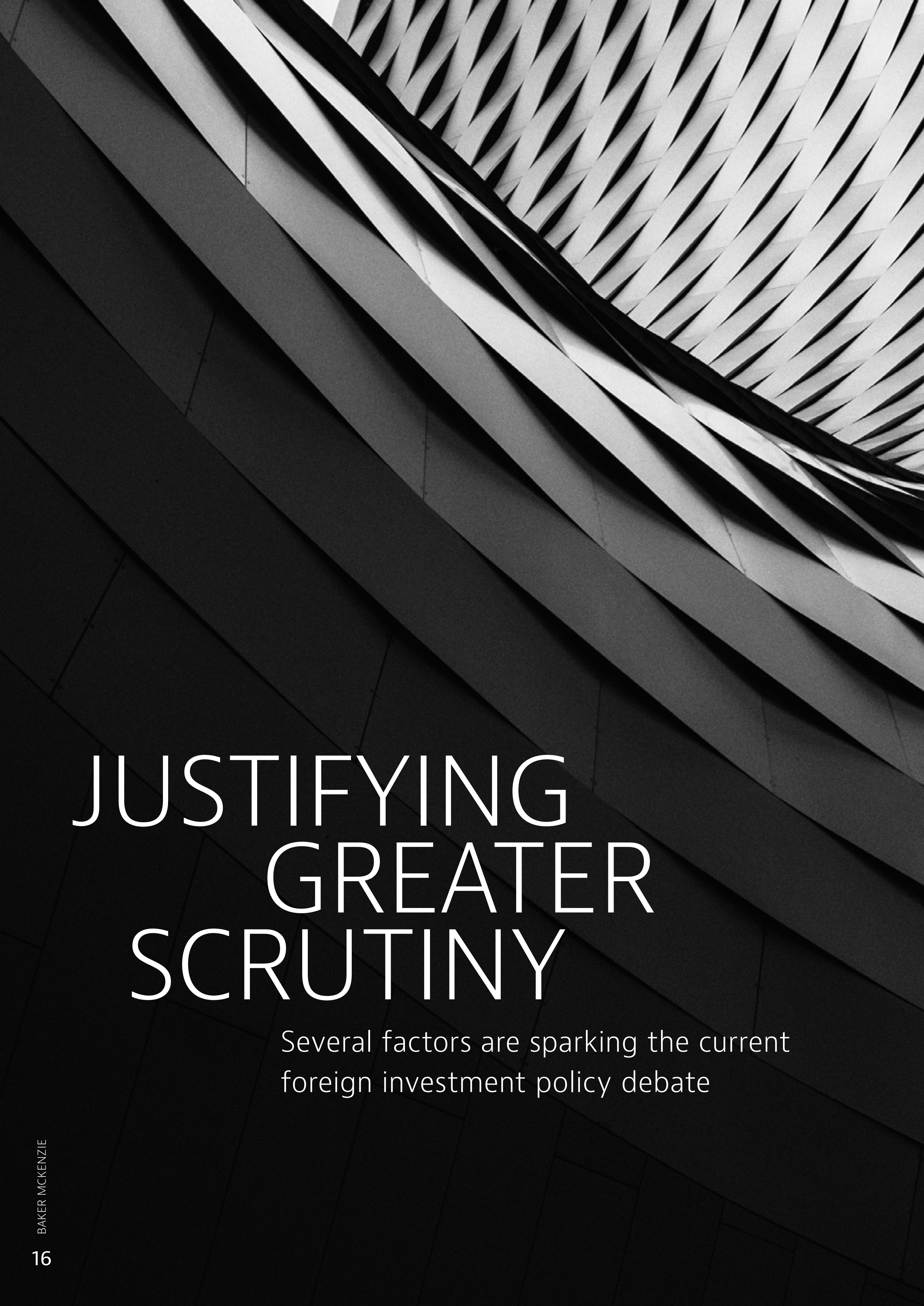
Investors that take the time to identify applicable foreign investment laws and a regulatory strategy early in the deal process can minimize the risk of delays, last-minute changes to the deal structure, or even failed transactions.



"CFIUS is often described as a black box. While far from a crystal box, the reality is that if you conduct a proper risk assessment early in the transaction by and large you know what you are getting into, you know what the issues are, and you can manage the risks."

SYLWIA LIS

Regulatory Partner, Baker McKenzie



JUSTIFYING GREATER SCRUTINY

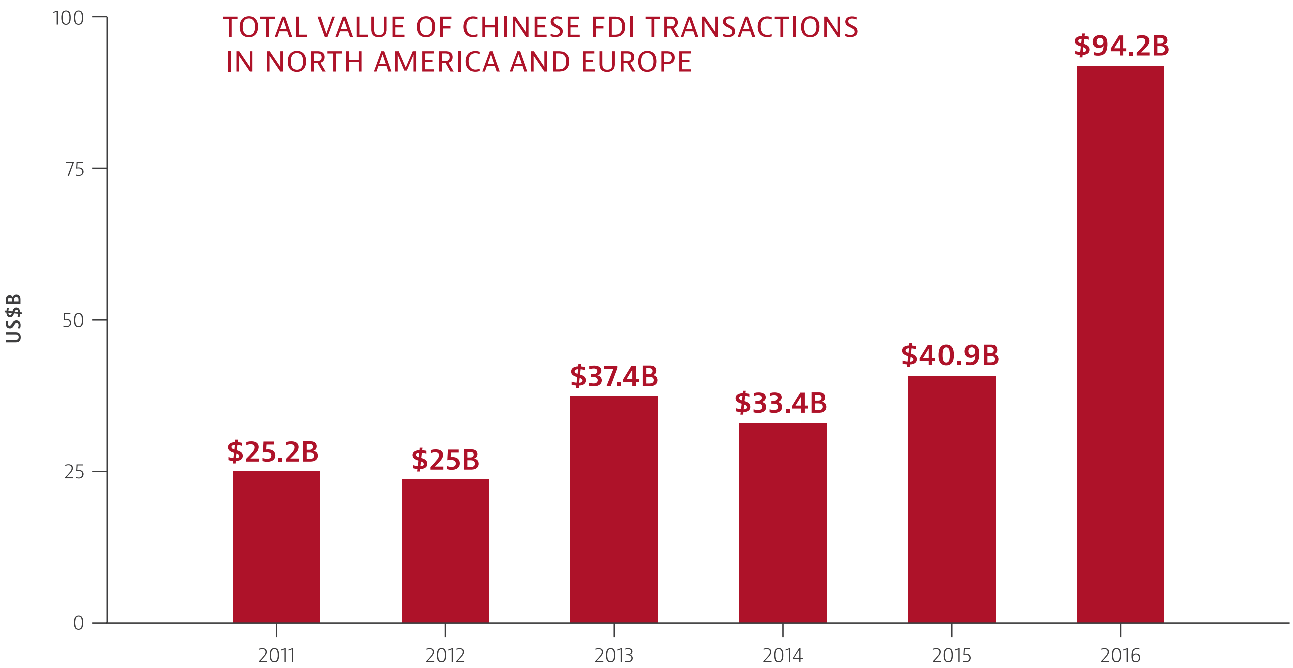
Several factors are sparking the current foreign investment policy debate

Foreign investment policy has not been immune to the sensitivities about globalization seen throughout the world. While globalization and technology have long been the driving forces of global economic growth, today the picture is complicated. The benefits of globalization have not flowed equally to all, and rising populism and nationalism are upending attitudes to inbound investment in many advanced economies. The localization and industrial policies of emerging markets are also provoking reactions in advanced markets.

Against this backdrop, politicians in some countries have voiced concerns about the economic and national security risks posed by foreign investment, including record levels of Chinese investment and increasing activity by state-owned enterprises and sovereign wealth funds. Large transactions, particularly foreign bids for well-known host country brands, have also generated controversy. These issues can be compounded by trade imbalances and claims of unequal market access. Below we discuss three of the key factors that are driving advanced economies to review their foreign investment frameworks.

1 Record levels of Chinese investment

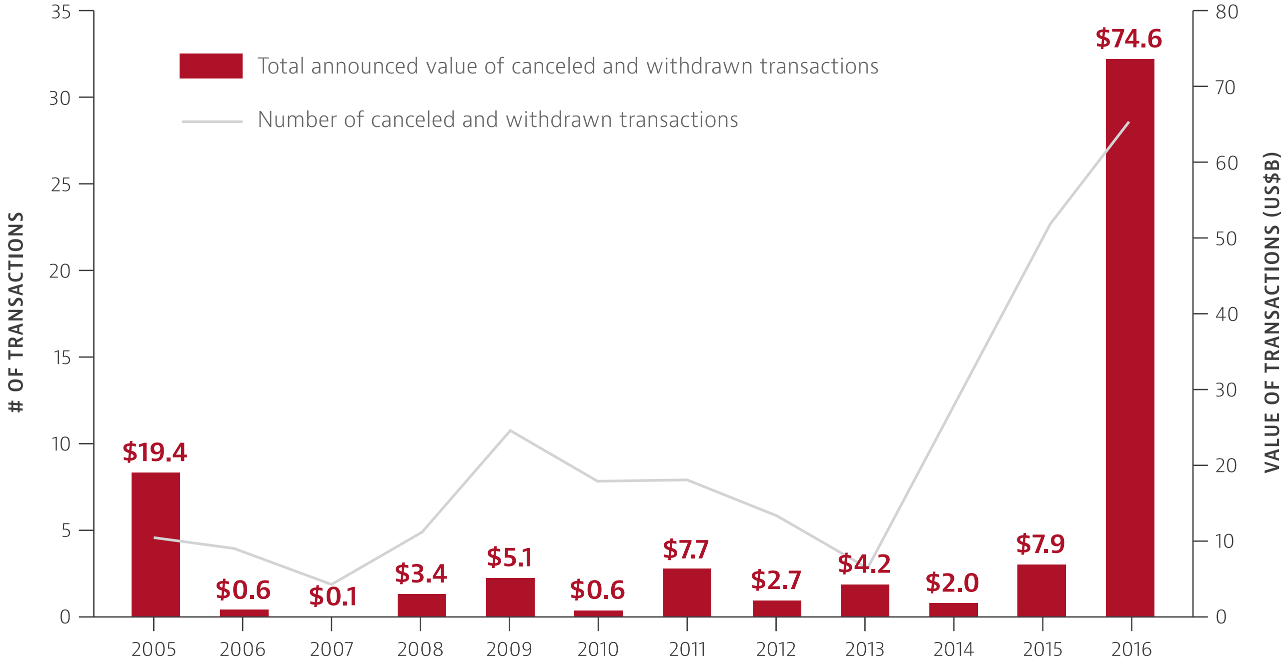
Chinese outbound investment hit another record high in 2016, rising to $200 billion globally. Chinese direct investment nearly tripled in North America and doubled in Europe, reaching a combined value of $94.2 billion in both regions, up 130% from $41 billion in 2015.[2] And while dealmaking fell in Q1 of 2017, largely due to China's crackdown on capital outflows, China was the second most acquisitive cross-border nation in Q2, with 94 deals valued at US$35.9 billion.[3]



Source: Rhodium Group. Data represents the combined value of direct investment transactions by Mainland Chinese companies, including greenfield projects and acquisitions that result in significant ownership control (>10% of equity). Europe includes the EU-28 and the European Free Trade Association (EFTA) countries: Iceland, Liechtenstein, Norway, and Switzerland. North America includes the United States and Canada.

[2] Baker McKenzie and Rhodium Group, Rising Influence: Assessing China's Record FDI Surge in North America and Europe (2017).
[3] Baker McKenzie Cross-Border M&A Index Q2 2017.

CANCELED AND WITHDRAWN CHINESE FDI TRANSACTIONS IN NORTH AMERICA AND EUROPE



Source: Rhodium Group

Chinese investment activity would have been even higher in 2016 if not for a significant rise in aborted transactions. In North America, for example, Chinese investors walked away from 10 deals worth $59 billion. In Europe, Chinese investors canceled or withdrew 20 deals worth $16.3 billion.[4] Although the rise in canceled transactions can be attributed to a much higher volume of announced transactions in 2015 and 2016 as well as purely commercial reasons, greater regulatory and political scrutiny in North America and Europe contributed to the increase.[5]

Over the last year, several developed countries have expanded government review of foreign investments in strategic sectors. For example, in July 2017, Germany extended the duration and scope of examination for investments in defense and other highly sensitive sectors following public and political debate over a number of Chinese acquisitions, including the acquisition of German robotics company Kuka by Beijing-based Midea Group.

In early 2016, on the heels of controversy surrounding China's Landbridge Group's 99-year lease of the Darwin Port for A$500 million, the Australian government mandated that all acquisitions of critical infrastructure assets (eg, ports, telecommunications, nuclear facilities, electricity, gas, water) be reviewed by its Foreign Investment Review Board. Since then it has blocked other deals, including the A$10 billion-plus sale of Ausgrid to China's State Grid Corporation and the A$370 million sale of S Kidman & Co, the country's largest private landholder, to a China-led consortium.

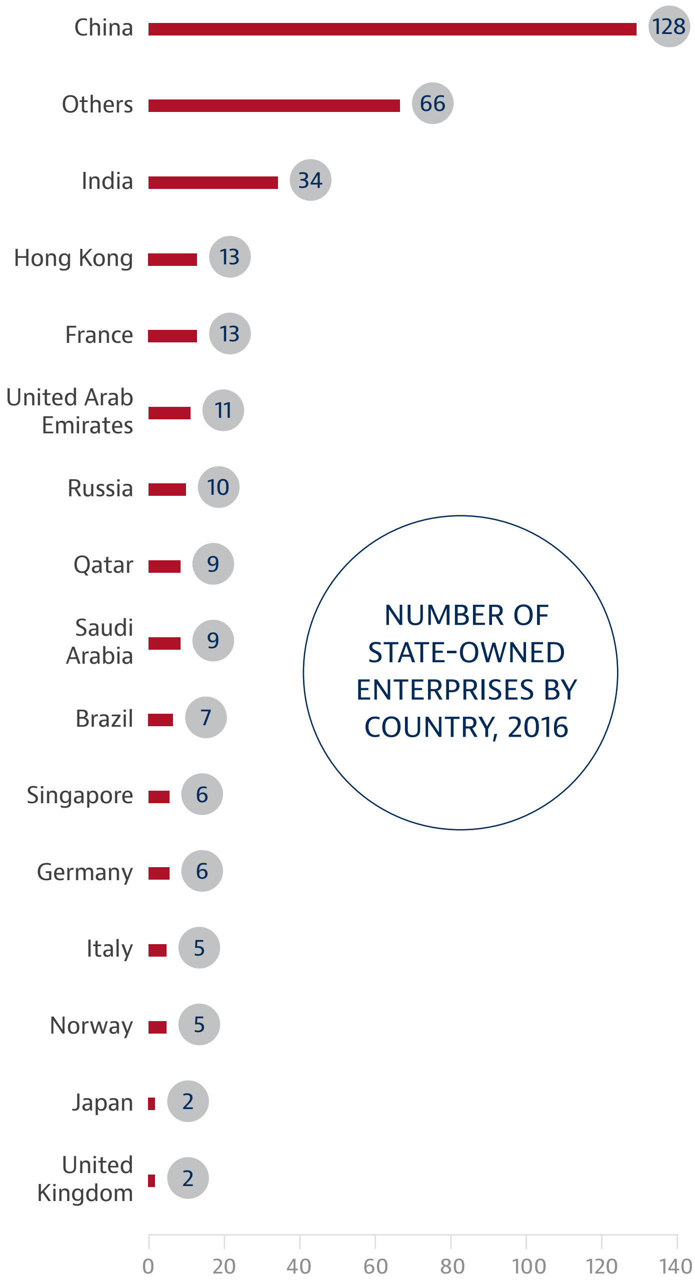
Other countries are considering legislative action to fill what they perceive to be national security holes in investment frameworks. In the US, Senator John Cornyn has introduced legislation to modernize how the Committee on Foreign Investment in the United States (CFIUS) screens investments to address his concern that China has "strategically weaponized investment and joint ventures" to obtain advanced US technology.

Similarly, at an EU level, politicians in the European Parliament – including those from France, Germany and Italy – have suggested stronger laws to restrict foreign investors from buying assets in key industries, amid growing fears that China and other countries may gain a competitive edge by buying European expertise while denying EU investors the same rights in their markets. However, other EU member states such as the Netherlands, Portugal and Spain have pushed back.

On 13 September 2017, European Commission president Jean-Claude Juncker confirmed that the EU will pursue a new framework for screening foreign investments. "Europe must always defend its strategic interests," Juncker said in his State of the Union speech. "If a foreign, state-owned, company wants to purchase a European harbor, part of our energy infrastructure, or a defense technology firm, this should only happen in transparency, with scrutiny and debate." While the proposed regulation does not directly make reciprocity a factor in deciding whether FDI raises security concerns, the recitals emphasize the need for vigorous and effective policies to open up other economies and ensure a level playing field.

2 Increasing activity by state-owned enterprises and sovereign wealth funds

It is estimated that 22 of the world's largest 100 firms are effectively under state control, the highest percentage in decades, according to a 2016 report by the Organisation for Economic Co-operation and Development (OECD). And many of these firms have been active foreign investors in recent years, contributing to unease in some host countries.



Source: Organisation for Economic Cooperation and Development.

[4] Baker McKenzie and Rhodium Group, Rising Influence: Assessing China's Record FDI Surge in North America and Europe (2017).
[5] Id.

A GROWING ROLE OF SO-MNEs IN THE GLOBAL ECONOMY

1,500 STATE-OWNED MNEs

86,000 FOREIGN AFFILIATES

Source: United Nations Conference on Trade and Development, World Investment Report: Investment and the Digital Economy (New York: United Nations 2017).

For example, state-owned enterprises have dominated China's global OFDI activities for most of the past decade, accounting for more than 70% of Chinese OFDI in Europe and North America from 2008 to 2013.[6] While private investors' share of investment in both geographies has gradually increased, and even overtook state investment in both regions in 2016,[7] the role of state-owned companies remains prominent. SOEs also led Chinese outbound investment in the first half of 2017.[8] Similarly, sovereign entities such as China Investment Corporation (CIC) and various entities affiliated with the State Administration of Foreign Exchange (SAFE) were early investors in Europe and now have a significant portfolio of direct investments in the region.[9]

This activity is sparking government concerns about the possible non-commercial motives of investors and their relationship to foreign government economic and geopolitical initiatives. Politicians and defense experts have pointed to potential security threats in the form of espionage, as well as the potential ability of state-related investors to influence host country politics and foreign policy. SOEs may also receive subsidies or other government incentives from their home countries, distorting the competitive landscape.

"The perception of some regulators, and the media, is that Chinese companies are willing to pay premiums that are prohibitive for other bidders to acquire assets of strategic importance," says Thomas Gilles, an M&A partner in Baker McKenzie's Frankfurt office.

While some countries such as Australia, Canada and the US already distinguish between foreign government-controlled investors and private investors for foreign investment review purposes, other advanced economies are considering new regulations to address the issue. For example, in early 2017, the German, French and Italian governments wrote to the European Commission arguing that EU member states should have broader latitude under EU law to block foreign transactions that are "unfair … because they rely on state funds or are aimed at buying up important technologies." The proposed EU regulation would allow the Commission and EU countries to take into account whether the foreign investor is controlled by a government of a third country, including through significant funding. Germany's Economic Affairs Minister Brigitte Zypries welcomed the Commission's proposals to ensure member states have "clear powers to intervene in the case of state-controlled direct investment in European companies."

"There is a view among some EU countries that they need to be able to react if investments are being made on the back of a political strategy and state-subsidized financing; however, I don't see a great deal of risk that the EU will be able to implement measures in the near term given the divergent views among member states and difficulties inherent in tracing money and putting a framework around private M&A transactions," says Gilles.

> “The perception of some regulators, and the media, is that Chinese companies are willing to pay premiums that are prohibitive for other bidders to acquire assets of strategic importance.”
>
> **THOMAS GILLES**
> M&A Partner, Baker McKenzie

3 Changing ideas about economic and national security

Advances in technology and evolving geopolitical risks are also leading some countries to think more broadly about national security and the ways in which it can be threatened. As a result, foreign investors need to be aware of foreign investment review challenges, even in sectors not typically associated with national security risk, such as healthcare and agriculture.

In recent years, some advanced economies have expanded the scope of national security concerns to encompass critical infrastructure and strategic sectors. For example, in an attempt to combat GE’s bid for Alstom in 2014, France extended the state’s veto scope from “national security and defense” to include its energy, water, transport, telecom and health sectors.

Australia has tightened its regulations governing foreign investments into critical infrastructure, housing and agriculture. Most recently, in January 2017, the government announced the establishment of a Critical Infrastructure Centre in response to what it identified as an increased risk of “sabotage, espionage and coercion”[10] related to Australia’s critical infrastructure facilities (e.g., telecommunications, electricity, water, ports).

Other countries are considering new laws to address potential threats. For instance, legislation introduced in the US Senate in March 2017 would add food security to the statutory list of factors that CFIUS must consider during its national security reviews.

More broadly, there is growing bipartisan consensus around legislation being drafted to modernize CFIUS to deal with “the current realities and tactics” of foreign governments.[11] Citing China’s Made in China 2025 initiative, which aims to turn the country into a global leader in advanced technologies, Senator Cornyn and other government and national security officials have expressed concern that China’s investments have the potential to undermine US defense capabilities.[12]

The UK government has also signaled that it plans to increase scrutiny of foreign investments that could impact national security, including foreign ownership of companies controlling critical infrastructure.

The draft EU regulation allows EU governments to prohibit investments of any kind by a foreign investor aimed at creating or maintaining lasting and direct links between the investor and the target. The implications are far-reaching, as “security and public order” concerns are widely interpreted to include effects on critical

[6] Baker McKenzie and Rodium Group, Bird’s Eye View: Comparing Chinese Outbound Investment in North America and Europe (2016).
[7] Baker McKenzie and Rhodium Group, Rising Influence: Assessing China’s Record FDI Surge in North America and Europe (2017).
[8] Thilo Hanemann, Adam Lysenko and Cassie Gao, Tectonic Shifts: Chinese Outbound M&A in 1H 2017 (Rhodium Group, June 27, 2017).
[9] Baker McKenzie and Rodium Group, Bird’s Eye View: Comparing Chinese Outbound Investment in North America and Europe (2016).
[10] Australian Government Critical Infrastructure Centre, Strengthening the National Security of Australia’s Critical Infrastructure: A Discussion Paper (2017).

infrastructure (energy, transport, communications, data storage, space, financial infrastructure, sensitive facilities); effects on critical technologies (artificial intelligence, robotics, semiconductors, dual use, cybersecurity, space, nuclear technology); effects on the security of supply of critical inputs (eg, mining outputs); and effects on access to or the ability to control sensitive information).[13]

The looming question is whether, and to what extent, nations decide to consider economic interests in screening investments, either explicitly or within the rubric of national security. While some countries currently evaluate the economic impact of foreign investment as part of the review process – for example, Canada's "net benefit" test – others have focused on sectors traditionally associated with national security. This may be changing.

In the US, for example, Senators Chuck Grassley and Sherrod Brown recently proposed legislation, the United States Foreign Investment Review Act of 2017 (S.1983), that would amend The Trade Act of 1974 and create a new screening procedure to vet economic implications for the US of particular foreign investments. This new procedure, which would operate in parallel to CFIUS, would authorize the Secretary of the US Department of Commerce to block or require the restructuring of certain transactions that could result in foreign control of US businesses. In making decisions, the Commerce Secretary would consider "economic factors," including "long-term strategic economic interests," "the history of distortive trade practices" of the investor's country of origin, and "any other factors the Secretary considers appropriate."[14]

Foreign bids for strong national brands have also generated media attention and controversy. For example, citing a foreign investor's unsuccessful bid for AstraZeneca, UK Prime Minister Theresa May has noted that some deals would benefit from closer scrutiny. According to May, "A proper industrial strategy wouldn't automatically stop the sale of British firms to foreign ones, but it should be capable of stepping in to defend a sector that is as important as pharmaceuticals is to Britain."[15] While May has shifted her focus to critical national infrastructure, stricter review of acquisitions of high profile or strategic host country assets could further complicate the foreign investment picture.

The looming question is whether, and to what extent, nations decide to consider economic interests in screening investments, either explicitly or within the rubric of national security.

—

[11] Council on Foreign Relations, Foreign Investments and National Security: A Conversation with Senator John Cornyn (June 22, 2017); https://www.cfr.org/event/foreign-investments-and-national-security-conversation-senator-john-cornyn.

[12] Id.

[13] http://www.bakermckenzie.com/en/insight/publications/2017/09/eu-control-foreign-investment/

[14] http://tradeblog.bakermckenzie.com/the-grassley-brown-bill-a-new-approach-to-foreign-investment-reviews/

[15] George Parker and Arash Massoudi, Theresa May to back new investment vetting system, Financial Times (Oct. 9, 2016); https://www.ft.com/content/773a9770-8e34-11e6-8df8-d3778b55a923; accessed on Sept. 9, 2017.

STRATEGIES TO CLOSE THE DEAL

Investors need to factor foreign investment review risks into M&A planning

Foreign investment is a hot-button issue in many advanced economies as governments respond to current economic and geopolitical conditions. The narrative of a foreign country "buying" another is not a good one for host country governments, and many politicians want to demonstrate activity in this area. Whether political positions will turn into legislative changes in certain countries remains to be seen.

Likewise, the impact of changes to foreign investment laws on M&A activity is not yet fully known. While the vast majority of transactions in the advanced economies covered in this report continue to be approved, uncertainty related to foreign investment review risk inevitably makes some buyers less attractive than others. All of this activity underscores the need for investors to prioritize foreign investment review risks.

"Right now, in North America, the foreign and national security regime is probably the more important conversation than the merger control discussion, which used to be the big one. What used to be somewhat of an afterthought, a form that the corporate lawyers would fill out after a transaction had closed, is a much more significant part of the risk assessment on a lot of transactions for our clients than it's ever been before," says Arlan Gates, an antitrust, competition and foreign investment partner in Baker McKenzie's Toronto office.

Below we offer 10 strategies to help foreign investors get the deal through.

1 Conduct an early risk assessment

Buyers should conduct a risk assessment as early as possible, certainly pre-approach, to determine if national security concerns exist. Not having a clear analysis to put forward to a seller undermines a purchaser's negotiation position, particularly in an auction sale or public bid context.

"If we come in as the purchaser with a better sense of the risk based on an independent review, we have an advantage when it comes to putting the deal together and getting it signed. We are more informed about possible outcomes, which helps in negotiating the deal terms and timeline, including the price and potential penalties for termination or abandonment if the transaction doesn't go forward," says Mike Fieweger, Chair of Baker McKenzie's Global Private Equity practice.

> "Before engaging in any new project, investors need to assess carefully its commercial viability. As governments tighten regulatory and legal requirements and scrutiny, Chinese investors in particular have to factor in the increasing cost of compliance."
>
> **BEE CHUN BOO**
>
> M&A Partner, Baker McKenzie
>
> Baker McKenzie, Belt and Road: Opportunity and Risk - The prospects and perils of building China's new Silk Road (2017); www.bakermckenzie.com/ChinaBRI

An early risk assessment can also help the purchaser negotiate the assistance of the target during the review process. "National security reviews can be demanding on the target due to information requests from government regulators," notes Craig Roeder, an M&A partner in Baker McKenzie's Chicago office. "It's helpful if the target has its eyes open and is willing to cooperate."

Understanding the challenges and coming in with a regulatory risk management strategy based on professional legal advice can also help buyers overcome challenges in the bidding process, including negative seller perceptions (whether justified or not).

"Before engaging in any new project, investors need to assess carefully its commercial viability. As governments tighten regulatory and legal requirements and scrutiny, Chinese investors in particular have to factor in the increasing cost of compliance," according to Bee Chun Boo, a partner in Baker McKenzie's Beijing office.[16]

2 Elevate national security risks for investors with any hint of a state-affiliation

In view of rising political and economic sensitivities, investors that are directly or indirectly government-owned, -controlled, or even -influenced should consider foreign investment review regulations as a threshold issue. Even private investors headquartered in countries with state-directed economies should expect elevated national security scrutiny.

"The question of whether a buyer is a state-owned enterprise can be murky. It bleeds over from ownership to interest very quickly because the moment you have any hint of foreign state involvement on some level – whether it's the source of money, involvement in governance, or even commercial dependence, such as the fact that a company in China is a supplier to the Chinese government – that can be enough to create the nexus of foreign government influence," says Gates. "Sometimes it's hard to distinguish what's state-directed from what's private."

While China features prominently in the headlines, large SOE investors from other emerging markets have also drawn attention in Canada, adds Gates.

Banks and private equity firms financing transactions may also encounter more scrutiny if they are themselves SOEs or subject to state influence, or may certainly be exposed if the target and/or purchaser raise these concerns.

> "The heavy presence of European companies in North America makes it increasingly important for foreign buyers to assess CFIUS-related risks for potential acquisitions of European targets with significant operations in the US."
>
> **SAMANTHA J. MOBLEY**
> Competition & Trade Partner, Baker McKenzie

3 Take a global view of national security risks

Early identification of impacted jurisdictions and cooperation between counsel on the strategy are paramount. Even minor operations or activities in a country with strong national security laws can potentially present roadblocks, and countries are increasingly likely to coordinate their national security review efforts.

A noteworthy example of such cooperation came last year when China's Fujian Grand Chip Investment Fund was seeking to acquire German chip equipment maker Aixtron, which had operations in the US. It was widely reported that after US government officials shared information with Germany about the security implications of the proposed acquisition, Germany reversed itself and declined to approve the transaction. Soon after, US President Obama also rejected the transaction, leading Fujian to drop its attempt to acquire the company.

[16] Baker McKenzie, Belt and Road: Opportunity and Risk - The prospects and perils of building China's new Silk Road (2017); www.bakermckenzie.com/ChinaBRI

"The heavy presence of European companies in North America makes it increasingly important for foreign buyers to assess CFIUS-related risks for potential acquisitions of European targets with significant operations in the US," says Samantha Mobley, a competition and trade partner in Baker McKenzie's London office.

Significantly, draft EU regulations would require EU governments to share information on foreign investments with each other and with the European Commission, and to state which investments they plan to screen. This requirement would also apply to EU countries that do not currently have a national review system. Individual member states would be able to raise concerns about foreign investment taking place in another member state. The European Commission could also give a non-binding opinion on such investments and carry out its own review of foreign investment that affects a project of EU interest, such as projects involving substantial EU funding or in relation to critical infrastructure, critical technology or critical inputs.

Monitoring political and foreign investment review issues in individual regions and countries is critical, but it is going to be just as important to understand the global regulatory implications of these developments. "One of the biggest implications of increased cooperation is the likelihood that competitors or disgruntled investors will be able to game the security reviews. The proposed EU regulation, for example, would create multiple entry points — the Commission, other EU institutions, and any other member state that considers itself affected. It's not too difficult to conjure up images of multijurisdictional campaigns to encourage the blocking of a foreign acquisition," says Rod Hunter, a trade and investment partner in Baker McKenzie's Washington, DC office.

4 Engage with the reviewing body early in the process

Most advanced economies, including Australia, Canada, France, Germany, Spain and the US, provide foreign investors with the opportunity to obtain formal or informal guidance from the reviewing authority in advance of an official filing. And a growing number of countries are encouraging investors to do so.

For example, the Canadian government issued guidance in 2016 encouraging investors to contact the Investment Review Division at the earliest stages of the development of their investment projects if there are potential national security concerns or questions.

Australia's Foreign Investment Review Board likewise encourages early engagement. "Engagement with FIRB at the outset is recommended and can be done informally, before any public announcement is made in order to minimize the risk of a deal not being passed. Ultimately, FIRB wants to encourage investment and will do all it can to help secure safe passage with the Australian Government, achieving Treasury approval," says Richard Lustig, a partner in Baker McKenzie's Melbourne office.

Foreign investors should work with counsel to engage with relevant officials up front, even on an informal basis without disclosing the client's name, to identify and quantify risks. Doing so can produce several benefits. "From a purely regulatory standpoint, the earlier you go in, the more receptive the regulators are likely to be because they feel you're being respectful. At the end, you're more likely to negotiate a favorable outcome than if you leave things to the last possible minute and take advantage of every statutory right," says Lis.

Early engagement can also help avoid government extensions, which can result in a longer waiting period. For example, in Canada, the government may extend the initial 45-day statutory period by an additional

45 days, and further extensions can lead to a review period of up to 200 days. "Sometimes giving the government a few extra days can enable them to work within the first 45-day screening deadline much more easily than if we surprised them," says Gates.

Similarly, maintaining a dialogue with the relevant body can help the parties to predict the timetable. This can help the corporate team structure the deal, including the timeline and process for diligence, closing steps, and transaction documentation. And, in a worst-case scenario, the informal review process can help the foreign investor to avoid the negative publicity and future deal impacts of being labeled a threat to national security.

5 Craft a public and government relations strategy

Foreign investment reviews can be highly political and susceptible to negative media attention, and developments on this front in one country can easily impact the perception and process in another.

"In one recent matter, a US firm with a competing bid mounted a media campaign in the host country in an attempt to get the government to overturn its decision and to attract CFIUS attention to the deal, despite the target having a limited US presence," recalls Hunter. "While our colleagues involved us early to craft a CFIUS strategy, and our cross-border team was able to get the deal through, the issue stayed alive in the media for some time, even after the US firm withdrew its bid."

Since the perception of a deal can be dictated by how it is covered by the press, foreign investors need to develop political and media strategies for potentially controversial transactions. These strategies should include strong messaging about issues such as how the transaction will benefit the host country workforce, economy and reputation in the global marketplace.

The Putzmeister-Sany transaction is an example of a well-executed press strategy. When German concrete pump maker Putzmeister was acquired by its Chinese competitor Sany in 2012, Putzmeister executives stressed that it would not lead to workforce reductions. They also noted that the acquisition would give the company much-needed funding to expand into western markets.

"Putzmeister told the media it wanted to be acquired by Sany and had reached a very good arrangement," says Christian Atzler, an M&A partner in Baker McKenzie's Frankfurt office who worked on the deal. "The executives stressed that it would provide a major boost to the company."

6 Understand the process and timeline

The process and time frame for screening investments can vary widely and may not be as predictable as statutory provisions suggest. The procedural complexities can be even greater for multi-jurisdictional deals. Foreign investors need global and local expertise to understand the substantive and procedural requirements in each jurisdiction, as well as the likely time frame for review.

For example, the prescribed time for CFIUS to review a transaction is 75 days – 30 days for review and a 45-day investigation period – but the process can take much longer. The clock doesn't start until the submission is deemed complete; the parties can refile if the initial 75-day review expires without a decision; and deadlines can be extended voluntarily.

"On balance, there is a consensus that the CFIUS process is taking longer and that investigations are becoming more laborious. We are seeing multiple rounds of questions, some of which are not strictly related to national security," says Hunter.

STATUTORY TIMELINES FOR REVIEW	
Australia	30-day examination period; 10-day notification period
Canada	Initial 45-day screening period, up to 200 days with extensions
France	2 months maximum
Germany	2 months; the Ministry may open a review within 5 years after the signing
Italy	15 days; possibility to extend once in case additional information is needed
Spain	30 days to 6 months
United Kingdom	N/A
United States	Initial 30-day review period, with a possible 45-day investigation

Foreign investors should also consider the process and timing in deciding whether to voluntarily file a notification or application. In the US, for example, if the foreign investor does not file a voluntary notification, CFIUS can review the transaction at any time and even recommend that the president unwind a completed transaction for national security reasons. In Germany, for investments in sectors not subject to mandatory filing or notification requirements, new rules expand the government's review period from three months to five years. As a result, more investors are likely to submit voluntary filings to avoid the uncertainty that the government could unwind the transaction or impose other requirements up to five years after the transaction has closed.

7 Be prepared to make detailed disclosures

Foreign buyers should engage early with legal advisers to understand the information likely to be requested and designate a point person to assist with information requests to avoid delays. Information requests from reviewing bodies can be detailed and seek sensitive details about the company, its products and services, its owners, and key individuals (e.g., directors, key executive officers, and certain shareholders). This includes the disclosure of any ownership, control, and/or management interests or rights in the acquirer, its intermediate parent and ultimate parent companies held by any agency or entity of a foreign government.

Similarly, requests can relate to customer information such as whether the investor provides goods or services to the host country government or any foreign government, including the specific governments, agencies, and goods and services provided.

8 Consider deal terms to allocate risk and responsibility

Foreign investors should involve regulatory counsel early in the deal to ensure risks are effectively addressed in the transaction agreement and throughout the deal.

For example, the buyer should ensure that the due diligence process allows it to fully understand the relationship of the target (and its subsidiaries and affiliates) with the host country government, including whether the target:

- provides (or has provided) any products or services to any host country government agency as a contractor or subcontractor
- has facilities or personnel with government security clearances
- has facilities located in proximity to sensitive government facilities

- produces or trades in any items controlled for export (e.g., US International Traffic in Arms Regulations)

To address regulatory uncertainty, more buyers and sellers are trying to quantify and allocate the risk between them, drawing on a menu of risk-shifting provisions. Options range from seller-friendly "hell or high water" clauses that require the buyer to pay the seller the agreed consideration for the target business even if the buyer is blocked from completing the acquisition, to commitments on how much effort the buyer is required to expend to obtain approvals.

"We're increasingly seeing the parties negotiate a reverse break fee to manage regulatory risks, whether in the host country or the buyer's home country," says Roeder. "These clauses can be useful if the buyer isn't prepared to take on the CFIUS risk or if the parties disagree on how big that risk is, particularly when the seller may be inclined to accept a lower bid from an alternative bidder with a perceived lower risk. The fee shows how far a buyer is willing to go to get a deal through while capping its liability. At the same time, it guarantees the seller compensation if the deal fails for national security reasons."

9 Consider mitigation measures as part of transaction strategy

As part of a regulatory strategy, particularly if risk factors are present, the parties should consider mitigation measures prior to filing a notification or application. Pre-filing consultations with the local authority can also help to identify what kind of actions might be required for approval. That can provide the time and space the parties need to work out what they may be willing to divest in a worst-case scenario, and even enable them to address the risk upfront by modifying the deal.

For example, pre-emptive divestitures may be appropriate if the target has defense contracts or other contracts relating to national security, develops or uses sensitive dual-use technologies, or has access to military facilities. Pre-filing mitigation measures may also make sense in a multi-jurisdictional deal where the target has limited operations in a sensitive jurisdiction. Carving those assets out may allow the rest of the deal to move forward smoothly.

10 Don't forget about other regulatory hurdles

Finally, other regulations and reporting requirements can apply to foreign investors depending on the transaction and must not be overlooked. These can include exchange controls, antitrust notification requirements, securities regulations, and merger control regulations, to name a few. Countries may also limit or even prohibit foreign ownership in certain industries such as defense, banking, energy or broadcasting.

Foreign investors should also identify required governmental licenses. Most businesses operate with a variety of licenses and permits (e.g., general business licenses, building permits, product registrations, environmental permits). These generally are not assignable even though material to the business. They may also terminate in the event of a material change in control of the target. If new licenses or permits need to be issued, the buyer will want to be certain it can obtain them prior to the closing in all relevant jurisdictions.

In some cases, regulations in the investor's country of origin can be a bigger factor in the transaction than those in the host country. "In my opinion, the decline in Chinese investment into Europe that we've seen this year has been more a result of tighter restrictions on the Chinese outbound side than on the European side," says Gilles.

> "We're increasingly seeing the parties negotiate a reverse break fee to manage regulatory risks, whether in the host country or the buyer's home country."
>
> **CRAIG ROEDER**
> M&A Partner, Baker McKenzie

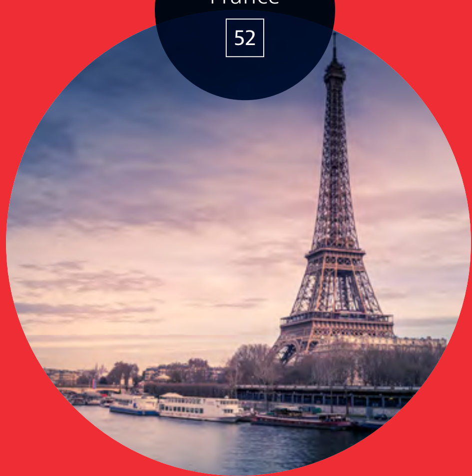
REGULATORY UPDATES

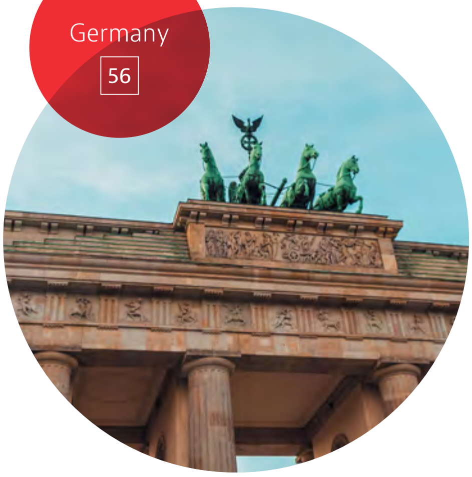
European Union 48

Italy 60

United Kingdom 64

France 52





Germany
56

Australia
34

Canada
38

United States
42

Spain
62

Australia

FOREIGN INVESTMENT ENVIRONMENT

Liberal

RELEVANT LAWS

Foreign Acquisition and Takeover Regulations 2015; Foreign Acquisitions and Takeovers Amendment (Exemption and Other Measures) Regulations 2017

REVIEWING BODY

Foreign Investment Review Board under the Ministry of Treasury

MOST SCRUTINIZED INDUSTRIES

Critical Infrastructure, Agriculture

REVIEW THRESHOLD

Yes

NATIONAL SECURITY DEFINITION

Not defined

OVERVIEW

Australia has a history of welcoming foreign investment, and deep ties to Asia. "Australia's economic prosperity is undoubtedly tied to Asia, and foreign direct investment flows from the region have been, and will continue to be, a reliable source of funds helping to grow Australia's GDP," says Richard Lustig, a partner in Baker McKenzie's Melbourne office. "At the same time, areas deemed to be 'critical infrastructure', particularly in the agricultural sector, will no doubt attract more scrutiny, making it critical for foreign investors to be aware of national security triggers."

Australia reformed its foreign investment framework in 2015 and again in 2017, in part to streamline the process and facilitate foreign investment. At the same time, the changes have strengthened the national security side of the review process. The recent appointment of a former top security official to the head of Australia's investment review board could signal another shift toward increased scrutiny of transactions related to critical infrastructure assets.

CURRENT REGIME

Foreign investment in Australia is regulated by the Foreign Acquisitions and Takeovers Act of 1975 (FATA)[17] and government policy. Under this framework, certain investments by a "foreign person"[18] require the approval of the Australian Treasurer through the Foreign Investment Review Board (FIRB).

Notification requirements vary and are based on a number of factors including whether the investor is a foreign government or non-government investor, the type of acquisition, whether the acquisition is subject to monetary thresholds, and FTA commitments. In general, FIRB approval is required for acquisitions of an interest of 20% or more in an Australian entity valued at more than AUD 252 million, investments in "sensitive" sectors (eg, media, telecommunications, transport, defense, and the extraction of uranium or plutonium or the operation of nuclear facilities) and investments in "Australian land" or an "Australian land corporation".

Direct investments by a foreign government must receive FIRB approval regardless of the dollar value, with few exceptions. These investments receive more scrutiny and may have separate conditions imposed as part of the approval process. FIRB considers a "foreign government" to include companies and other legal entities in which a foreign government has more than a 20% interest, or companies and other legal entities that are otherwise controlled by the foreign government, such as SOEs and sovereign wealth funds.

SCORECARD

IS THE AUSTRALIAN GOVERNMENT TIGHTENING FOREIGN INVESTMENT REVIEWS? Yes

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS?

New legislation

FOREIGN INVESTMENT REVIEWS

120,272 applications considered (2012-13 to 2015-16)

REJECTIONS

8 applications rejected (2012-13 to 2015-16)

In determining whether an investment is contrary to the national interest, FIRB considers factors such as the impact of the investment on Australia's ability to protect its strategic and security interests, whether the investment may result in an investor gaining control over market pricing and production, the effect on tax revenues, the impact on the economy and community, and the character of the investor.

FIRB approvals are generally granted within 30-40 days; however, the Treasurer has the option to extend review by 90 days. A failure to file a notification may result in substantial fines or imprisonment for the acquirer and/or a divestiture order if the acquisition is deemed to be contrary to the Australian national interest.

[17] Separate legislation imposes other requirements and/or limits on foreign investment in various sectors such as banking, airports, shipping, and telecoms.

[18] A foreign person includes a natural person not ordinarily a resident in Australia, a foreign corporation or trust, or an Australian corporation or trust in which a foreign person holds a substantial interest (20% alone or two or more foreign persons who hold a 40% interest).

RECENT DEVELOPMENTS

While Australia's foreign investment review framework has long been geared toward facilitating foreign investment, recent changes signal a greater focus on national security interests.

In response to an increasing number of state and territory asset privatizations, in 2016, the government amended FATA to remove the exemption for private foreign investors acquiring an interest in critical infrastructure assets purchased directly from state and territory governments.

In addition, in January 2017, the government announced the establishment of the Critical Infrastructure Centre (CIC) to manage national security risks to Australia's critical infrastructure assets, with an initial focus on telecommunications, electricity, water, and ports. Critical infrastructure is defined as "those physical facilities, supply chains, information technologies and communication networks which, if destroyed, degraded or rendered unavailable for an extended period, would significantly impact the social or economic wellbeing of the nation or affect Australia's ability to conduct national defense and ensure national security."[19] The CIC is also charged with developing and maintaining a critical assets register that will help FIRB to assess and provide feedback on whether an application is likely to trigger more scrutiny.

The appointment of David Irvine, former director-general of the Australian Security Organization and the Australia Secret Intelligence Service, to the role of FIRB Chairman is another move widely seen as increasing scrutiny of foreign bids for sensitive assets.

At the same time, as part of its 2017-18 budget, the government announced changes to simplify foreign investment regulations and the fee framework. For example, amendments that took effect in July 2017:

- introduced new business exemption certificates, including for foreign government investors;
- increased notification thresholds for global transactions holding Australian interests;
- amended the treatment of residential land used for commercial purposes (which will benefit investors interested in student accommodation, aged care facilities and retirement villages);
- narrowed the scope of non-vacant commercial land treated as sensitive;
- clarified the treatment of developed solar and wind farms; and
- allowed for multiple approvals for similar low risk transactions.

Foreign buyers should continue to benefit from Australia's open foreign investment policies and efforts to modernize and streamline its framework. However, investors targeting infrastructure assets can expect more scrutiny as the government responds to what it has identified as an increased risk of "sabotage, espionage and coercion"[20] related to Australia's critical infrastructure facilities.

> "Australia's economic prosperity is undoubtedly tied to Asia, and foreign direct investment flows from the region have been, and will continue to be, a reliable source of funds helping to grow Australia's GDP."
>
> **RICHARD LUSTIG**
>
> Corporate Partner, Baker McKenzie

APPLICATIONS CONSIDERED: 2012–13 TO 2015–16 (NUMBER OF PROPOSALS)				
Outcome	2012–13 No.	2013–14 No.	2014–15 No.	2015–16 No.
Approved without conditions	5,535	12,307	21,355	26,954
Approved with conditions	7,196	11,795	16,598	14,491
Total approved	**12,731**	**24,102**	**37,953**	**41,445**
Rejected	-	3	-	5
Total decided	**12,731**	**24,105**	**37,953**	**41,450**
Withdrawn	446	719	799	1319
Exempt	145	181	180	244
Total considered	**13,322**	**25,005**	**38,932**	**43,013**

Source: FIRB 2015-16 Annual Report.

Note: Figures include corporate reorganisations (99 in 2015-16). This data is excluded in other approvals analysis unless otherwise noted.

2015–16 fiigures were impacted by the 1 December 2015 reforms, which may impact comparability of data. The 2014–15 figures have also been revised.

[19] Australian Government Critical Infrastructure Centre, Strengthening the National Security of Australia's Critical Infrastructure: A Discussion Paper (2017).

[20] Id.

Canada

OVERVIEW

Canada has long been open to foreign investment, and the Trudeau government appears to be signaling a more liberal approach to foreign investment reviews. It has significantly raised review thresholds for direct investments by private investors from WTO- and EU-member states, as well as some other states with which Canada has trade agreements, authorized a previously blocked investment from China, and issued guidance on its approach to national security reviews, providing greater transparency to foreign investors.

At the same time, public and political concerns have surfaced in the face of recent acquisitions, including Chinese-based Hytera Communications Co. Ltd.'s takeover of Vancouver-based Norsat. Despite a national security screening process lasting three months, some commentators expressed concern that a formal national security review leading to the imposition of conditions on the transaction was never ordered. Norsat makes satellite communications technology used by the US military and other NATO partners. In response, the US Department of Defense said it would review its business dealings with Norsat.

FOREIGN INVESTMENT ENVIRONMENT

Liberal

RELEVANT LAWS

Investment Canada Act

REVIEWING BODY

Investment Review Division of Innovation, Science and Economic Development and Governor in Council

MOST SCRUTINIZED INDUSTRIES

Defense, Telecommunications (Equipment and Networks), Uranium Mining, Critical Infrastructure

REVIEW THRESHOLD

No

NATIONAL SECURITY DEFINITION

Not defined

"We are seeing more transactions that may affect multiple countries from a national security standpoint. How to reconcile Canada's interests with concerns of allies is becoming a bigger issue, which can have spillover effects on the parties to the transaction," says Arlan Gates, an antitrust, competition and foreign investment partner in Baker McKenzie's Toronto office.

While Canada is open for business, foreign investors, particularly those with any level of foreign state involvement, need to assess national security risks early in the transaction.

CURRENT REGIME

The Investment Canada Act (ICA) requires non-Canadian investors who acquire control of a Canadian business to submit either a notification or an application for review, depending on whether the investment exceeds applicable monetary thresholds. The thresholds (certain of which are adjusted annually) differ depending on characteristics of the investor and the investment, such as whether the acquisition is direct or indirect, whether the buyer is a WTO or EU investor or a state-owned enterprise, and whether the target is a cultural business.

SCORECARD

IS THE CANADIAN GOVERNMENT TIGHTENING FOREIGN INVESTMENT REVIEWS? Yes

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS?

Stricter enforcement

FOREIGN INVESTMENT REVIEWS

81 applications; 3,364 notifications

REJECTIONS

3 blocked; 5 divestitures; 4 subject to conditions before implementation (FY2012-17)[21]

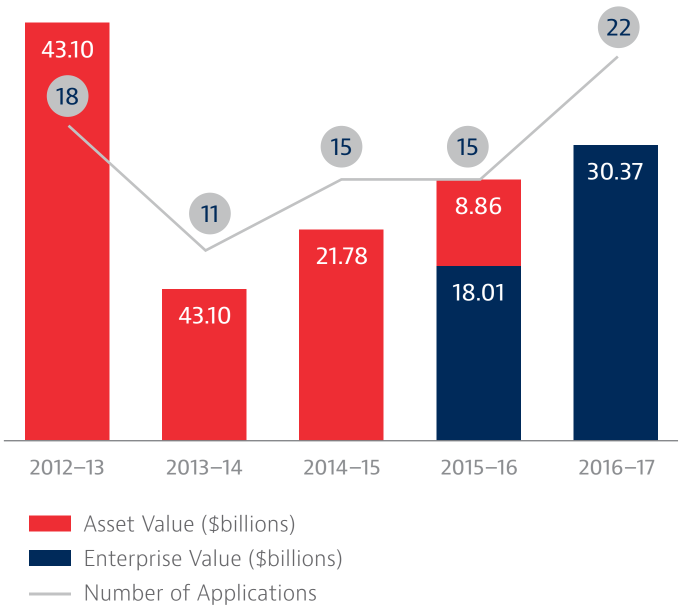
If review thresholds are exceeded, the non-Canadian must file an application for review with the Investment Review Division (IRD) prior to implementation of the investment. The Minister of Innovation, Science and Economic Development (or Minister of Canadian Heritage for transactions involving cultural businesses) has up to 45 calendar days to determine whether the investment should be approved as a "net benefit to Canada".

FISCAL YEAR (FY) 2016–2017 ORDERS IN HISTORICAL CONTEXT

	FY2012–13	FY2013–14	FY2014–15	FY2015–16	FY2016–17
s.25.3 order for review	2	1	4	1	5
s.25.4 final order	1 blocked	1 blocked	1 divestiture 1 blocked 2 conditions imposed	1 divestiture	3 divestiture 2 conditions imposed
Withdrawal following s.25.3 order for review	1				

Source: Innovation, Science and Economic Development Canada, 2015-16 Annual Report.

[21] Innovation, Science and Economic Development Canada, 2015-16 Annual Report on the Investment Canada Act (August 2017) at 1, available online: <www.ic.gc.ca/eic/site/ica-lic.nsf/eng/h_lk81126.html>



The minister may unilaterally extend the period by an additional 30 calendar days. For all other acquisitions of control and establishment of new businesses, non-Canadians must file a notification with the IRD no later than 30 days after closing or implementation.

The ICA also provides the government with the right to review any investments that "could be injurious to national security" irrespective of size, whether or not they involve the acquisition of a controlling interest and even if they only have a tenuous connection with Canada.

The Minister has 45 days (which can be extended by up to an additional 45 days) after an application or notification has been certified, or after the closing or implementation of an investment, whichever is later, to assess whether a proposed investment raises national security concerns and refer an investment to the Governor in Council (GIC) for an order for national security review. If the GIC decides to order a full national security review, and it is determined that a transaction poses a threat, the GIC may require written undertakings or specific terms and conditions, disallow the investment in whole or in part, or even unwind a completed transaction. The full national security review process may take up to 200 days.

While the ICA does not define what types of investments might be "injurious to national security", guidelines issued in 2016 are instructive. Among other factors, the government may consider:

- the effect on Canada's defense capabilities
- transfers of sensitive technology or know-how outside of Canada
- involvement in the research, manufacture or sale of controlled goods/technology
- impact on critical infrastructure
- the enablement of foreign surveillance or espionage
- the hindering of intelligence or law enforcement operations
- the potential involvement of illicit actors, such as terrorists or organized crime
- the impact on the supply of critical goods and services to Canadians and the federal government
- the impact of an investment on Canada's international interests or foreign relationships

This guidance is consistent with public information about the approximately dozen investments subjected to a GIC-ordered national security review during the period from 2012 through 2016. In practice, investors from countries part of the Five Eyes intelligence alliance with Canada – Australia, New Zealand, UK and the US – generally do not present concerns. On the other hand, buyers from China, the Middle East and countries subject to sanctions may attract more scrutiny.

In addition, the investments reviewed have generally been connected with a sensitive industry sector such as telecommunications, advanced technology and uranium mining. In one case, while the target's business did not appear to be sensitive, it was located near a sensitive government facility.

The 2016 guidelines also changed investor expectations about how to deal with potential issues by encouraging parties to transactions with one or more of these factors to engage early with officials. "The government wants to be involved before the deal closes," says Gates. "If a deal has certain features, we often start the prescreening process pre-closing or even pre-signing. If the 45 days are triggered and elapse, we are home free. If there are issues, we can address them pre-closing and adjust the structure of the transaction if necessary. Even informal discussions with the IRD can help to pave the way and provide a negotiating advantage to the purchaser."

RECENT DEVELOPMENTS

The Trudeau government has taken active steps to start a new chapter in Canada's foreign investment relationship with other countries. At the same time, there is increasing scrutiny of certain transactions based on who the investor is and what they're buying.

In April 2017, citing the importance of foreign investment to job creation, the government increased the threshold for pre-closing reviews for direct investments involving acquisitions of Canadian (non-cultural) businesses by WTO members to CAD 1 billion in enterprise value. It also increased the review threshold for direct acquisitions by SOEs from CAD 375 million to CAD 379 million.

The CAD 5 million threshold for direct acquisitions (CAD 50 million for indirect) related to cultural businesses or involving non-WTO members continues to apply. Indirect investments by WTO investors, including SOEs, also continue to be exempt from pre-closing review regardless of size.

In addition, as part of the measures being taken to implement the Comprehensive Economic and Trade Agreement (CETA) with the European Union, the ICA was recently amended to increase the threshold for review of acquisitions by investors from CETA countries (and certain other countries with which Canada has free trade agreements) to CAD 1.5 billion.

While these changes will further reduce the number of non-Canadian investments subject to government "net benefit" review, investments must still clear the national security hurdle. "All investments are scrutinized, and those with a national security dimension lead to questions. That is a matter of course now," says Gates. "Hytera, which was one of two headline deals in this space last year, highlights that even a deal with several risk factors can be green-lighted, but in borderline cases the outcome can be impacted by the extent to which the parties are proactive, cooperative and forthcoming. When in doubt, we go in."

> "We are seeing more transactions that may affect multiple countries from a national security standpoint. How to reconcile Canada's interests with concerns of allies is becoming a bigger issue, which can have spillover effects on the parties to the transaction,"
>
> **ARLAN GATES**
>
> Antitrust, Competition and Foreign Investment Partner, Baker McKenzie

United States

OVERVIEW

The US is characterized by a general absence of exchange controls and licensing of foreign acquisitions. Some regulations, however, apply to acquisitions of US companies by non-US entities. In particular, the Committee on Foreign Investment in the United States (CFIUS), an inter-agency committee of the US government, is authorized to review transactions that result in foreign control of a US business on national security grounds. In a few sectors, there are additional investment procedures and restrictions (eg, telecommunications and air carriers).

While the authority and operation of CFIUS have remained unchanged for over a decade, members of Congress are currently developing legislation to modify the US foreign investment review process. Legislators and executive branch officials have voiced concerns about the transfer of cutting-edge technology to foreign governments, as well as unequal treatment of US investors abroad, in response to growing investment from China and other countries.

While the trajectory for any legislative amendments remains unclear, the practical implications of certain proposals, if enacted,

> "Regardless of whether we see new legislation, given rising political and economic sensitivities, foreign acquirers need to engage on CFIUS-related issues early to manage risks."
>
> **ROD HUNTER**
>
> International Commercial Partner, Baker McKenzie

SCORECARD

IS THE US GOVERNMENT TIGHTENING FOREIGN INVESTMENT REVIEWS? Yes

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS?

Stricter enforcement

FOREIGN INVESTMENT REVIEWS

942 notices, 389 investigations, 107 total notices withdrawn

REJECTIONS: 2

Committee on Foreign Investment in the United States, Annual Report to Congress CY2015; Covered Transactions, Withdrawals, and Presidential Decisions 2014-2016

would be far reaching. For example, legislation being developed would significantly expand the range of transactions reviewed by CFIUS to include joint ventures of US firms with foreign entities (including those overseas), as well as passive investments where the foreign buyer may gain access to certain information regarding, for instance, critical technologies or infrastructure.

Even under the current framework, some investments are attracting more scrutiny. CFIUS's most recent annual report to Congress covering 2015 highlights an increase in the volume and complexity of CFIUS reviews. These trends are continuing in 2017. Under the Trump administration, CFIUS reviews are taking longer, with more and broader questions about buyers' and sellers' businesses and prior transactions and signs that transactions are being reviewed in the context of the larger geopolitical and industrial policy concerns.

"Regardless of whether we see new legislation, given rising political and economic sensitivities, foreign acquirers need to engage on CFIUS-related issues early to manage risks," says Rod Hunter. "Where transactions involve assets in multiple jurisdictions, potentially triggering multiple investment reviews, up-front engagement is all the more critical. Coordination between advanced economy regulators is on the rise."

CURRENT REGIME

CFIUS's mandate covers virtually all forms of acquisitions where a change in ownership or operational control over part or all of an entity or assets occurs. Even the transfer of control over a US business between two foreign companies can be subject to CFIUS review. In addition, the concept of "control" is broadly defined to include the power, whether direct or indirect, exercised or not, to determine important matters affecting the entity.

If CFIUS determines that a transaction may pose a threat to US national security, the committee may impose conditions on the transaction to mitigate national security risks it has identified, or recommend that the President of the United States block the transaction in whole or in part, or even unwind a completed transaction that has closed without a CFIUS review.

Although CFIUS's review is characterized as voluntary, CFIUS may commence a review on its own initiative (even after a transaction has closed). Once completed, a CFIUS review generally provides a "safe harbor" for the transaction.

Significantly, CFIUS regulations provide an illustrative, open-ended definition of "national security", which leaves CFIUS with maximum latitude to conduct its review. Moreover, the president's determinations are largely beyond judicial review. Based on the regulations and past transactions scrutinized by CFIUS, the following should be considered:

"Apart from possible legislative changes, we have seen a tightening of the CFIUS process as the volume of transactions has increased and the Trump Administration formulates its policy. Investors, particularly those from China, need to be aware of foreign investment review challenges even in sectors not typically associated with national security risk."

SYLWIA LIS

International Commercial Partner, Baker McKenzie

FOREIGN INVESTMENT ENVIRONMENT

Liberal

RELEVANT LAWS

Exon-Florio Amendment to the Defense Production Act of 1950 (1988); Foreign Investment and National Security Act of 2007 (FINSA)

REVIEWING BODY

Committee on Foreign Investment in the United States (CFIUS)

MOST SCRUTINIZED INDUSTRIES

Defense, Infrastructure, Information Technology & Communications

REVIEW THRESHOLD

No

NATIONAL SECURITY DEFINITION

Not defined; broad in practice

CHARACTERISTICS OF US BUSINESS BEING TRANSFERRED

The Committee is interested in transactions involving US businesses that:

- provide products and services to federal, state, or local authorities, especially those related to defense, security or law enforcement, or involving information technology, telecommunications, energy, or natural resources
- engage in the production of advanced technologies that may be useful in defending or seeking to impair US national security, including the design and production of semiconductors and other products with dual commercial and military applications, or the provision of goods or services such as cryptography, data protection, internet security and network intrusion detection
- participate in the US energy sector, including businesses that hold major energy assets or are involved in exploitation of natural resources, transportation or transmission of power
- affect US transportation system, including maritime and shipping, port terminal operations, and aviation
- engage in research and development, production or sale of technology, goods, software or services subject to restrictions under US export controls
- operate close to sensitive US military facilities
- have access to classified information

COVERED TRANSACTIONS, WITHDRAWALS, AND PRESIDENTIAL DECISIONS: 2009–2016									
Year	2009	2010	2011	2012	2013	2014	2015	2016	**Total**
Number of Notices	65	93	111	114	97	147	143	172	**942**
Number of Investigations	25	35	40	45	48	51	66	79	**389**
Total Notices Withdrawn	7	12	6	22	8	12	13	27	**107**
Presidential Decisions	0	0	0	1	0	0	0	1	**2**

Source: Committee on Foreign Investment in the United States, Annual Report to Congress CY2015; Covered Transactions, Withdrawals, and Presidential Decisions 2014-2016.

CHARACTERISTICS OF BUYER

The Committee is interested in transactions involving:

- buyers from countries or regions perceived as sensitive from the US national security standpoint, particularly where the buyers are owned or controlled by the foreign government
- foreign parties having track record of actions that could impair US national security, including plans to terminate contracts between the US business and the US government
- foreign government-controlled parties, including foreign government agencies, state-owned enterprises, government pension funds and sovereign wealth funds
- foreign parties from countries with poor records on non-proliferation and other national security-related matters

RECENT DEVELOPMENTS

Prompted by the significant uptick in foreign direct investment from China, several Senators and House members are exploring amendments to CFIUS. In late 2016, several members tasked the Government Accountability Office with conducting an assessment of the US review process, and in the waning days of the Obama administration an outgoing scientific advisory committee raised concerns about Chinese industrial policies in critical technologies such as semiconductors.

Similar concerns have been voiced by Defense Secretary James Mattias, Chairman of the Joint Chiefs of Staff General Joe Dunford, Director of National Intelligence Dan Coats, CIA Director Mike Pompeo, NSA Director Michael Rogers and members of the Senate Select Committee on Intelligence and Senate Armed Services Committee. There is a growing consensus that the current CFIUS process does not consider the range of investment decisions made by countries into key technology companies, including venture capital deals involving companies with early stage technologies.

Republican Senator John Cornyn, together with a bi-partisan group of co-sponsors, proposed a CFIUS bill, the Foreign Investment Risk Review Modernization Act (FIRRMA), that would maintain a focus on national security, but would expand CFIUS's jurisdiction to reach, for example:

- Joint ventures and other "arrangement[s]" between US critical technology companies and foreign investors, even outside of the US and
- Real estate sales and leases proximate to sensitive US government sites.

The bill would arguably broaden the definition of "control" - and hence the scope of CFIUS's jurisdiction - from an interest providing the ability to shape management and personnel decisions of the US business to even mere access to non-public information. While CFIUS would have authority to exclude certain investments from allied countries, the bill's changes would encompass many transactions not previously within the ambit of CFIUS, including US investments in China, Indonesia, and other emerging markets that impose technology transfer obligations and even largely financial transactions in the US.

In addition, FIRRMA would create a mandatory declaration procedure for certain foreign investments in US businesses. In particular, the declaration obligation would apply to certain investments by state-owned enterprises and investments in certain US critical technology companies, including those with "emerging technologies." The declaration process, with its simplified (five page) filings, would provide CFIUS with the opportunity to decide whether to require a regular CFIUS notification or simply allow the transaction to proceed.

FIRRMA would also marginally extend the current CFIUS timelines and would create a user-fee system where parties filing notifications (but not declarations) would pay fees that would be used to fund CFIUS's operations.

"CFIUS is increasingly becoming a technology control regime, and the Cornyn bill would continue that trend. Indeed, the legislation would direct CFIUS to work with allied governments to develop similar regimes aimed at controlling the flow of cutting edge technologies with security implications, a response to policies of major emerging markets. While the United States continues to maintain an open investment policy, foreign investors – especially those from China – need to be aware of the investment screening challenges even in sectors not traditionally associated with national security," says Rod Hunter, a regulatory partner in the Washington, DC office. "Most transactions do not encounter insurmountable obstacles, but there can be significant timing implications. It is critical to assess regulatory risks early in a transaction's lifecycle."

Significantly, CFIUS regulations provide an illustrative, open-ended definition of “national security”, which leaves CFIUS with maximum latitude to conduct its review.

—

European Union

OVERVIEW

The EU has proposed a new EU framework for screening foreign investment that raises "security or public order" concerns for the EU or its member states. The proposal does not go as far as obliging member states to adopt their own national screening systems, but confirms that member states that do have such regimes must comply with the proposed EU requirements, in order to ensure greater coordination and transparency. The European Commission itself will not have the power to block foreign investments.

The latest move by the EU is in line with steps taken by European governments to tighten control over foreign acquisitions of critical national assets. Businesses that are considering investing in the EU may increasingly need to assess whether their investments raise security or public order concerns and if so, carefully consider their notification strategies in the relevant EU countries.

FOREIGN INVESTMENT ENVIRONMENT

Liberal.

RELEVANT LAWS

N/A

REVIEWING BODY

N/A

MOST SCRUTINIZED INDUSTRIES

N/A

REVIEW THRESHOLD

No

NATIONAL SECURITY DEFINITION

Not defined; although the proposals set out a non-exhaustive list including critical infrastructure, critical technologies, security of supply of critical inputs and access to sensitive information or the ability to control sensitive information.

CURRENT REGIME

While the EU market is generally open to foreign investment, a comprehensive EU regime for controlling or screening foreign investment does not exist. Many EU countries have their own national regimes to screen deals that raise national security concerns, and the current approach to foreign investment screening in the EU is marked by a patchwork of member state laws, if any, which vary in scope and criteria.

RECENT DEVELOPMENTS

Under the proposed EU framework, national screening mechanisms must be transparent and meet basic EU requirements. Member states must (i) specify the trigger and grounds for screening as well as relevant procedural rules, (ii) establish timeframes for issuing screening decisions, (iii) protect confidential information, and (iv) allow for the possibility of judicial review against screening decisions.

The EU proposal provides guidance on the factors that member states may take into account in deciding whether a foreign direct investment raises "security or public order" concerns. Member states may take into account the potential effects on:

- critical infrastructure, including energy, transport, communications, data storage, space or financial infrastructure, as well as sensitive facilities;
- critical technologies, including artificial intelligence, robotics, semiconductors, technologies with potential dual-use applications, cybersecurity, space or nuclear technology;
- the security of supply of critical inputs; or
- access to sensitive information or the ability to control sensitive information.

SCORECARD

IS THE EU TIGHTENING FOREIGN INVESTMENT REVIEWS? Yes

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS?

A new EU framework has been proposed, but the proposal must still pass the legislative procedure.

This is a non-exhaustive list, so member states remain free to further broaden its scope.

The European Commission will also have the power to carry out its own screening of foreign direct investment that is "likely to affect projects or programmes of Union interest". Such projects must (i) involve a significant share of EU funding, or (ii) relate to Union legislation and critical areas of infrastructure, technologies or inputs. Indicative examples include the Galileo and EGNOS satellite programs and transport, energy and telecoms infrastructure under the EU Trans-European Network programs. The European Commission itself will not be able to block the foreign investment but will have 25 working days to give its opinion. While the opinion will not be binding, member states are required to "take utmost account" of it and provide an explanation if they do not follow it.

The EU proposal is a reaction to the security concerns raised by recent foreign investment activities by non-EU investors. After a series of acquisitions of European companies by state-owned or controlled foreign investors, especially from China, concerns were voiced as to whether key technologies and infrastructures critical for society and economy in the EU were sufficiently protected. Member states such as France, Germany and

Italy further requested reciprocal investment rights and called for EU regulation to ensure a level-playing field in international business.

Whilst the draft EU regulation does not go as far as expressly making reciprocity a factor in deciding whether a foreign investment raises security concerns, the recitals and accompanying communication state the need for vigorous and effective policies to open up other economies and ensure that everyone plays by the same rules. Furthermore, in deciding whether foreign investment raises security concerns, the European Commission and EU countries may take into account whether the foreign investor is controlled by a government of a third country, including through significant funding.

The EU proposal provides that EU governments will be able to prohibit foreign investments that fall short of acquisitions of control. The screening will apply to investments of any kind by a foreign investor aimed at creating or maintaining lasting and direct links between the foreign investor and the target, including investments which enable effective participation in the management of a business. Only portfolio investments are expressly excluded in the accompanying explanatory documents. The new framework will apply to EU member states only.

EU governments will be required to share information on foreign investments with each other and with the European Commission, and to state which investments they plan to screen. Individual member states will be able to raise concerns about foreign investment taking place in another member state. The European Commission will also have the power to give a non-binding opinion on such investments.

President Juncker indicated that the European Commission intends to launch, and possibly complete, the proposed framework by the end of 2018. France, Germany and Italy have issued a joint statement welcoming the EU's proposals as an important step towards a level playing field in Europe. It is worth noting, though, that several member states (such as the Netherlands, Portugal and Spain) have opposed increased scrutiny...and at this stage, it is unclear whether the proposal will be approved by the EU Council.

The latest move by the EU is in line with steps taken by European governments to tighten control over foreign acquisitions of critical national assets.

—

France

OVERVIEW

Generally, the French legal system encourages foreign investment, with no statutory limits on foreign ownership of companies. Foreign companies have access to a wide range of financial incentives and the number of bureaucratic formalities foreign companies face have decreased significantly in recent years. However, the French government has long held the position that there should be more protective measures in place to ensure EU firms enjoy the same benefits abroad.

With a stable legal environment, substantial resources and quality infrastructure, France attracted over $28 billion in FDI last year, of which $2.4 billion came from China. Between 2000 and 2016, France saw $14.2 billion of FDI from China with several significant deals that received strong media attention. The most noteworthy of these were the purchase of a stake in GDF Suez for $3.2 billion in 2011, and the acquisition of Louvre Hotels for $1.6 billion in 2015.

French President Emmanuel Macron has vowed to form a more protective Europe as concern grows over Chinese acquisitions in the EU's strategic industries. During the EU summit, Macron worked to convince his counterparts that stricter controls over foreign investments should be put into place. In February 2017, Italy, Germany and France proposed that the EU Commission investigate more closely when foreign investment is involved in strategic sectors.

CURRENT REGIME

The foreign investment regime was modified in May 2014 with the Montebourg Decree. This expanded the sectors in which the state has control over foreign investment. In these listed sensitive sectors, foreign investors must file for prior authorization from the Minister of Economy (MoE).

When an investment falls under the conditions of the prior authorization requirement, a request for clearance must be filed and the clearance obtained prior to closing the transaction. This obligation to file for clearance lies with the investor. If there is uncertainty over whether prior authorization is required, the foreign investor may request a prior confirmation from the MoE. A response to the request may take up to two months from receipt of all necessary information. It is important to note that a lack of response is not an indication that authorization is not required.

To request authorization of a transaction, the investor should send all relevant documents to the Treasury Department of the MoE. The request should consist of three originals and include detailed information about the investment, investor, its shareholders and the target company/business, especially the sensitive activity at stake.

The amount of time it takes for the MoE to issue a decision regarding the investment is two months maximum. During the review process, the MoE may involve other relevant ministries depending on the sector at stake. There are three possible outcomes to the prior authorization request: authorization of the transaction without covenants, authorization of the transaction subject to mitigating covenants, or refusal to grant authorization. "Refusals are very rare in our experience," says Guillaume Nataf, partner in Baker McKenzie's Paris office.

SCORECARD

IS THE FRENCH GOVERNMENT TIGHTENING FOREIGN INVESTMENT REVIEWS?

Yes

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS?

NEW LEGISLATION - Montebourg Decree dated 14 May 2014

If the MoE finds that a foreign investment has been completed without the required prior authorization, despite a refusal from the MoE, or in breach of the covenants, the MoE may order the investor to stop, modify or annul the operation – in the latter case, ordering the investor that the previous situation be reinstated at its own expenses. If the investor does not comply with said order, the MoE may impose on the investor a monetary penalty up to twice the amount of the investment. Such orders and monetary penalty are subject to full review (*recours de plein contentieux*) before the French administrative courts. In cases of conditional authorization, the conditions must be proportionate to the risk to national interests.

Criminal sanctions may also apply. In particular, under the French Customs Code, any investment made without the required authorization, or any breach of the conditions to the authorization exposes the foreign investor to a maximum of five years imprisonment and a fine of up to twice the amount of the investment for an individual, ten times for a legal entity.

RECENT DEVELOPMENTS

Fueled by French voters' concerns about globalization, French President Emmanuel Macron promised to promote a more protective Europe at the EU summit in June 2017. Macron claimed that while foreign investors benefit from the EU's open market, European companies lack access to foreign markets, particularly China.

Together with Italy and Germany, France called for a EU mechanism to veto acquisitions by non-EU investors in strategic sectors. With strong opposition from countries such as Spain and Greece, the EU summit concluded with the decision that the EU Commission should analyze investments from third countries in strategic sectors, while fully respecting member states' competencies.

FOREIGN INVESTMENT ENVIRONMENT

Liberal

RELEVANT LAWS

Codified under Article R153-1 and seq. of the French Financial and Monetary Code; Montebourg Decree dated 14 May 2014 expanded the sectors in which foreign investment reviews are required.

REVIEWING BODY

Ministry of Economy, with assistance from other ministries if necessary

MOST SCRUTINIZED INDUSTRIES

Sectors deemed sensitive listed below

REVIEW THRESHOLD: No

NATIONAL SECURITY DEFINITION

Foreign investments made by a Non-EU investor in the following "sensitive" sectors require prior authorization from the MoE:

1 Gambling sectors (with the exception of casinos).

2 Private security regulated services.

3 Research, development or production of means aimed at fighting the illegal use, in connection with terrorist activities, of pathogenic and toxic substances and preventing the health consequences of such use.

4 Activities related to equipment used for interception communication and remote detection of conversations.

5 Services in connection with evaluation and certification of security of information technology products and systems.

6 Activities of production of goods or services provision of security in the information systems' security sector of a company that entered into a contract with a public or private operator managing facilities.

7 Activities relating to dual-use items or technologies.

8 Activities relating to the means of cryptology and services of cryptology.

9 Activities exercised by companies' custodians of secret of national defense including classified markets of national defense or of security clauses.

10 Activities of research, production or trade of weapons, ammunition, powder and explosive substances for military purposes or war equipment.

11 Activities exercised by companies having concluded a contract of research or of supply of equipment for the French Ministry of Defense, either directly, or through subcontractors.

12 Other activities relating to equipment, products or services, including those relating to the safety and the proper functioning of facilities and equipment, essential to guarantee the French national interests in terms of public policy, public security or national defense (these new sectors which include energy, transport, water, public health and telecommunications were introduced by the Montebourg Decree).

French President Emmanuel Macron has vowed to form a more protective Europe as concern grows over Chinese acquisitions in the EU's strategic industries.

—

Germany

OVERVIEW

Germany has long embraced foreign investment, imposing few limits on foreign investors and offering them the same rights and benefits as domestic acquirers. Between 2008 and October 2016, for example, the Ministry for Economic Affairs and Energy has conducted 335 foreign investment reviews, has issued few restrictions with regard to some of these investments, but has rejected none.

But this level of openness has been challenged over the years by key investments pursued by acquirers from the US, the Middle East and, more recently, China. From 2000 to 2016, Chinese foreign direct investment in Germany totaled USD 22.4 billion, second only to the UK among EU countries most targeted by Chinese acquirers.

In 2016 Germany overtook the UK as the biggest target market for Chinese investment, with total deal value rising nearly tenfold to USD 12.1 billion, up from USD 1.3 billion in 2015. The most significant of these acquisitions was Chinese appliance maker Midea's purchase of German robot manufacturer Kuka for USD 4.7 billion – the largest Chinese takeover of a German company ever.

FOREIGN INVESTMENT ENVIRONMENT

Liberal. Foreign investors have the same rights and benefits as German investors.

RELEVANT LAWS

Foreign Trade and Payments Act (2004)

REVIEWING BODY

Ministry for Economic Affairs and Energy

MOST SCRUTINIZED INDUSTRIES

Defense, IT security

REVIEW THRESHOLD

No

NATIONAL SECURITY DEFINITION

Two standards:

1. Mandatory reviews of acquisitions in the defense or IT security sectors: poses a "threat to material security interests of the Federal Republic of Germany"

2. Non-mandatory reviews in all other industries: poses a "threat to the German public security and order"

The Kuka deal sparked controversy in the German press, fueled by concerns that a rising number of crown jewels of German industry were falling into foreign hands at a time when the Chinese government continues to restrict foreign acquisitions in its market. As a result, the economy ministers of Germany, France and Italy wrote a letter to the European Commission in February 2017 urging the Commission to impose greater restrictions on investors whose home markets do not offer the same level of access.

> "The foreign investment landscape in Europe is shifting, and it is likely that regulatory change at EU level will occur."
>
> **JOACHIM SCHERER**
>
> Public Law Partner, Baker McKenzie

"The letter from the ministers is not about limiting investment in strategic industries or concerns about national security," says Joachim Scherer, a public law partner in Baker McKenzie's Frankfurt office. "It's about German companies wanting to be able to do the same direct foreign investment in China as the Chinese are allowed to do here."

SCORECARD

IS THE GERMAN GOVERNMENT TIGHTENING FOREIGN INVESTMENT REVIEWS? Yes

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS?

New legislation

FOREIGN INVESTMENT REVIEWS: 335

REJECTIONS: 0

(Source: data from 2008 to Oct 2016, table on page 58)

CURRENT REGIME

Concerns about rising Chinese investment also prompted the German government to adopt new regulations in July 2017 that expand the types of investments subject to mandatory review in Germany's defense sector. The new law also imposes notification requirements on investors in areas considered to be highly sensitive, such as companies that develop critical software for financial and telecom services, public transportation and power girds.

For investments in sectors not subject to mandatory filing or notification requirements, the new rules expand the government's review period from three months to five years. Previously, the German government could only intervene in these investments within three months after the deal was signed, even in cases in which the government wasn't aware of the transaction. "Now the timeframe in which the authorities can intervene has been expanded to five years after signing, allowing the authorities to unwind or impose other restrictions during

INVESTMENTS THAT UNDERWENT FOREIGN INVESTMENT REVIEW									
Year	2008	2009	2010	2011	2012	2013	2014	2015	10/2016
Restricted Sectors	2	6	4	6	6	3	6	3	1
General Threat to National Security	/	23	41	34	39	38	51	38	34

Source: Letter from the Secretary of State, Matthias Machnig, to Kerstin Andreae, a member of the German Bundestag.

this period of time. To address the legal uncertainty that comes with this extension, we will be seeing many more so-called applications for certificates of non-objection, a well-established route to obtain written and binding confirmation by the authorities that the acquisition does not raise any concerns," says Anahita Thoms, an international trade compliance partner in Baker McKenzie's Düsseldorf office.

These new regulations build on Germany's 2004 Foreign Trade and Payments Act, which gives the government the power to restrict foreign acquisitions in the defense and IT security industries that pose a threat to its "material security interests". In 2009, the law was amended to require mandatory foreign investment review of transactions in these sectors.

Aside from the defense and IT security sectors, the German government's ability to restrict foreign investment is constrained by EU trade law. To block foreign acquisitions outside of these sectors, German regulators must prove the transaction poses a threat to public order or public security. Moreover, what constitutes a threat to public order and security has been narrowly defined by the European Court of Justice (ECJ).

Under longstanding ECJ case law, EU member states can only block foreign investment from another EU member state if the target company is active in business sectors that would be relevant in times of crisis, such as energy suppliers and telecom network operators.

"Under the EU treaty, it's very difficult to restrict one EU company from acquiring shares in another EU company," says Julia Pfeil, a public law senior associate in Baker McKenzie's Frankfurt office. "It's one of the most basic founding principles that movement of capital should be free and equal throughout the EU."

This free and equal principal might seem like it would not apply to foreign investors outside the EU, but in practice it does. For tax reasons, many foreign acquirers establish special purpose vehicles in the EU, often in the Netherlands, to make acquisitions. As a result, the acquirer becomes a Dutch entity, which gives it the same rights as other EU businesses under the EU treaty.

RECENT DEVELOPMENTS

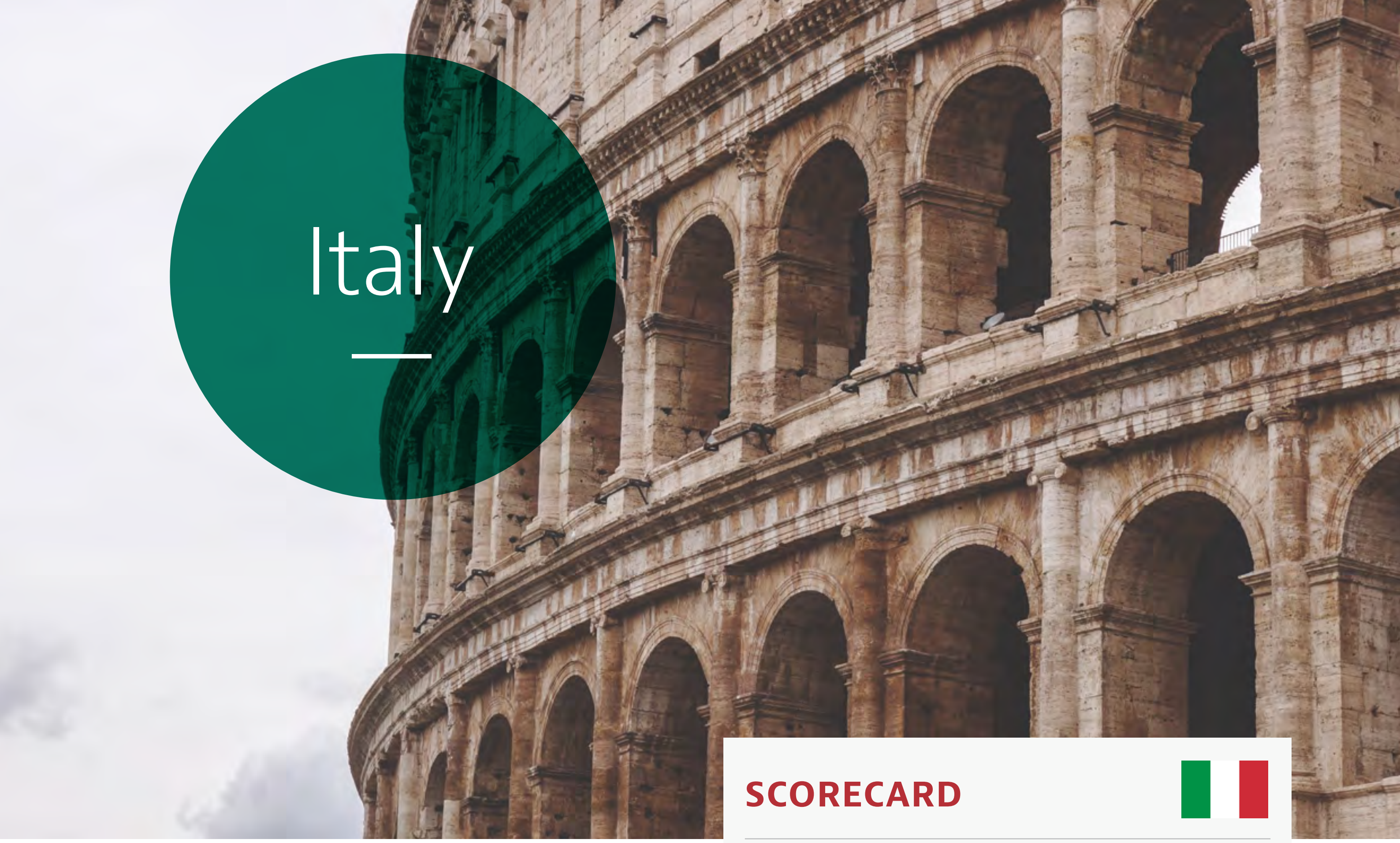
Recent media coverage of large Chinese acquisitions, the ministers' joint letter to the European Commission, and Germany's new regulations to control foreign investment have created an environment of greater scrutiny. In 2016, Germany's Ministry for Economic Affairs and Energy withdrew its approval of a transaction for the first time ever.

The ministry had initially issued a certificate of non-objection to Chinese investor Fujian Grand Chip's acquisition of Aixtron, a German semiconductor maker. Then in October 2016, under pressure from the US, the ministry withdrew that approval until regulators could review the transaction further. Two months later, former US President Barack Obama issued an executive order blocking the transaction on national security grounds.

Since then, Chancellor Angela Merkel has indicated that the EU Council of Ministers may discuss the possibility of an EU-wide screening of foreign investment in strategic sectors at its meeting this fall. This follows a similar initiative backed by French President Emmanuel Macron that gained support among many EU leaders but fell short of getting a consensus at the Council's summit in June.

"The foreign investment landscape in Europe is shifting, and it is likely that regulatory change at EU level will occur," Scherer says.

> "To address the legal uncertainty that comes with this extension, we will be seeing many more so-called applications for certificates of non-objection, a well-established route to obtain written and binding confirmation by the authorities that the acquisition does not raise any concerns."
>
> **ANAHITA THOMS**
>
> International Trade Compliance Partner, Baker McKenzie



Italy

SCORECARD

IS THE ITALIAN GOVERNMENT TIGHTENING FOREIGN INVESTMENT REVIEWS? No

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS? N/A

> "Italy is very open to foreign investment. There is a strong sentiment that whoever is most capable should do the job, regardless of nationality."
>
> **AURELIO GIOVANNELLI**
>
> Corpoarate and Commercial Partner, Baker McKenzie

OVERVIEW

In 2014, the Italian government brought forward the implementation process for Law No. 56 dated 11 May 2012. The new law was established to replace the old "Golden Share" of the Italian government with "Special Powers" regarding transactions entailing a threat of a serious harm to the essential interests of national defense and homeland security and to the operation of networks and plants and to the continuity of supplies in the energy, transportation and communications sectors. This change was put in place after strong criticism from the European Union that "Golden Share" was too restrictive and prevented the free movement of capital in the EU. Special Powers effectively loosened restrictions on foreign investment in Italy.

FOREIGN INVESTMENT ENVIRONMENT: Liberal

RELEVANT LAWS

- Law No. 56 dated 11 May 2012 setting forth the main features of the Special Powers in the defense, homeland security, energy, transportation and communications sectors;
- Decree of the President of the Council of Ministers No. 108 dated 6 June 2014 and Presidential Decree No. 35 dated 19 February 2014 identifying, respectively, the strategic assets and activities subject to the Special Powers in the national defense and homeland security sectors and the procedures and resources for the exercise of the Special Powers in the same sectors;
- Presidential Decree No. 85 dated 25 March 2014 and Presidential Decree No. 86 dated 25 March 2014 identifying, respectively, the strategic assets and activities subject to the Special Powers in the energy, transportation and communications sectors and the procedures and resources for the exercise of the Special Powers in the same sectors.

REVIEWING BODY: Office of the Prime Minister

MOST SCRUTINIZED INDUSTRIES

Defense, homeland security, communications, energy and transportation

REVIEW THRESHOLD: No

NATIONAL SECURITY DEFINITION

Law No. 56 dated 11 May 2012 does not provide a definition of "national security"; rather, it delegates the Prime Minister to adopt one or more decrees aimed at identifying the strategic activities subject to the Special Powers in the defense and national security sector. Indeed, by Decree No. 108/2014 the President of the Council of Ministers "reconciled the rules on the national defense and homeland security with the rules on the communications sectors, by specifically identifying the strategic activities as well as the key strategic activities to be subject to the Special Powers", say Raffaele Giarda and Antonio Lattanzio, partner and senior associate in Baker McKenzie's Rome office.

CURRENT REGIME

Pursuant to Law No. 56/2012, the Prime Minister may exercise Special Powers in relation to defense, homeland security, energy, transportation and communications sectors. Transactions involving assets in these sectors should be reported to the Office of the Prime Minister for prior authorization. The Prime Minister has 15 days to veto the transactions or impose conditions on the transaction that mitigate associated risks. This deadline can be extended once in case additional information is required. Upon expiry of the term, the transaction at stake is deemed approved.

Through the implementation process, several decrees were established to clearly define the strategic activities and assets in the defense, homeland security, energy, transportation and communications sectors subject to Special Powers. This significantly clarified the reference framework for international investors.

RECENT DEVELOPMENTS

Italy joined Germany and France in proposing that the EU Commission establish a mechanism to veto acquisitions by non-EU investors in strategic sectors. Concerns from Italy stem from the general principle of reciprocity that governs foreign investments. According to the Italian Civil Code, a foreign company is allowed to enjoy the same rights available to an Italian entity in the respective country.

Spain

FOREIGN INVESTMENT ENVIRONMENT

Liberal

RELEVANT LAWS

Law 18/1992 of July 1

MOST SCRUTINIZED INDUSTRIES

National defense-related activities, gambling, television, radio, and air transportation

REVIEW THRESHOLD: No

NATIONAL SECURITY DEFINITION

Not defined

OVERVIEW

The Spanish government recognizes the importance of foreign investment to its economy and maintains a favorable legal framework for foreign investors. The foreign investment review regime is generally liberal and does not distinguish between European (EU) residents and non-EU residents.

In an effort to attract foreign investment and strengthen the Spanish economy, Prime Minister Mariano Rajoy continues to emphasize the importance of making Spain a friendly destination for foreign investors. There have been no recent regulatory changes to increase scrutiny of foreign investments.

CURRENT REGIME

RESTRICTED INDUSTRIES

With the exception of a few sectors, there are no restrictions on foreign investments in Spain. Sectors subject to special regulations are national defense-related activities (including the exploitation of minerals of strategic interest and telecommunication services), gambling, television and radio, air transportation, telecommunications and energy.

Reviewing bodies and regulation vary depending on the industry sector, type of investment and in some cases, nationality of the investor. Foreign investments in activities directly related to national defense, such as manufacturing or trade of weapons, ammunition and military equipment are restricted and must be approved by the Council of Ministers.

In the television and radio sector, foreign investment restrictions and reciprocity principles apply for non-EU investments in broadcasters who offer their services via terrestrial hertzian waves ("DTT") (ie, a license is required and (i) the licensee must have its registered offices in a member state of the European Economic Area ("EEA") or a country that recognizes the same rights to Spanish companies under local legislation; (ii) the share capital of non-EEA individuals or entities must comply with the principle of reciprocity; (iii) the participation of any individual or entity from non-EEA countries may not directly or indirectly exceed 25% of the share capital; and (iv) the share capital in the broadcaster held by all individuals or entities from non-EEA must be less than 50%).

In addition, the acquisition of a relevant shareholding, either directly or indirectly, in Spanish financial institutions, such as banks, insurance companies or investment firms above a certain threshold (generally a minimum of 10% of the capital or voting rights of the relevant entity) is subject to prior authorization or, non-opposition by the relevant supervisory authority (Bank of Spain, General Directorate of Insurance and Pension Funds or Spanish National Securities Market Commission.

REPORTING OBLIGATIONS

All foreign investments in Spain must be reported to the registry of foreign investments (*Direccion General de Comercio e Inversiones*, or DGCI) for statistical, administrative or economic purposes. Generally, this process does not hinder or delay the financial transaction.

There are two regimes for reporting foreign investments to the DGCI:

1 Ex ante

In general, foreign investments in Spain are only required to be declared to the DGCI after the investment has been completed. As an exception, any projected foreign investment in Spain from territories that qualify as tax havens under the Spanish law must be declared by the investor, prior to the investment. The declaration carries a six-month validity, after which should the investment not be carried out, a new declaration must be done.

A prior declaration is not the equivalent to a verification or clearance and, once an investment is declared, the investor can carry out the transaction.

The following cases are exempt from prior declaration:

- Investment in listed securities or in securities that have been object of a public offering.
- Investment in listed shares or investment funds registered with the Spanish Securities Exchange Commission (CNMV).
- The foreign investment in a Spanish company does not exceed 50% of its share capital, neither prior nor after the projected investment

2 Ex post

With the exceptions mentioned above, foreign investments in Spain are typically required to be declared to the DGCI after the transaction.

SCORECARD

IS THE SPANISH GOVERNMENT TIGHTENING FOREIGN INVESTMENT REVIEWS? No

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS? N/A

RECENT DEVELOPMENTS

Spain has strongly opposed recent efforts from Italy, Germany and France to establish an EU mechanism to veto acquisitions by non-EU investors in strategic sectors.

United Kingdom

OVERVIEW

The UK has adopted an approach of welcoming foreign investment, with an absence of specific foreign investment controls and regulations. Many key sectors in the UK involve foreign investors, including energy, water and telecommunications. However, the UK government can and has intervened in certain cases on the grounds of specific public interest criteria.

In 2016, in part due to concerns around the USD 23 billion Hinkley Point nuclear power plant project (to be built and financed jointly by China and France) and calls for greater intervention in foreign acquisitions of UK businesses, the government announced plans to introduce foreign investment rules for critical infrastructure. As a result, in October 2017 the UK government published proposals for a new national security and infrastructure investment review regime.[22]

What this new regime will look like remains to be seen. Nevertheless, the UK's concerns over foreign ownership of UK assets relating to national security are not unique, and similar concerns have been raised in other EU jurisdictions, as well as at EU level.

FOREIGN INVESTMENT ENVIRONMENT

Liberal

RELEVANT LAWS

No specific regulation of foreign investors (General merger control laws apply to foreign and UK investors)

REVIEWING BODY

None; the Competition and Markets Authority is responsible for merger control

MOST SCRUTINIZED INDUSTRIES

Defense, telecommunications, media

REVIEW THRESHOLD

No

NATIONAL SECURITY DEFINITION

Not defined; includes "public security". In practice, interventions have generally concerned military equipment or related technology

[22] https://www.gov.uk/government/consultations/national-security-and-infrastructure-investment-review

CURRENT REGIME

There are currently no specific legal controls, based on nationality, of foreign investors in the UK (other than money laundering regulations). Foreign investors are subject to the same merger control rules as British investors.

Currently, the UK Competition and Markets Authority (CMA) has jurisdiction over mergers that meet either a financial or share of supply threshold. Filing for prior clearance is not mandatory and there is no need to wait for clearance from the CMA before closing a deal during the initial stage of the review process.

In exceptional cases, the UK government can intervene on the grounds of specified public interest criteria. These criteria are currently limited to national security, media plurality and stability of the UK financial system (there are also limitations on certain mergers between water companies).

The UK secretary of state may ask the CMA to examine a merger on any of these three public interest grounds, in addition to looking at the competition law considerations.

In addition, the secretary of state may also intervene in certain public interest cases where the merger jurisdictional thresholds are not met ("special public interest mergers"). These special public interest mergers are limited to (i) defense industry mergers if at least one of the enterprises concerned is carried on in the UK by, or under the control of, a body corporate incorporated in the UK and where one or more of the enterprises concerned is a relevant government contractor (ie, a contractor who has been notified by or on behalf of the secretary of state of information, documents or other articles relating to defense and of a confidential nature), or (ii) where the merger involves a supplier or suppliers of at least 25% of any description of newspapers or broadcasting in the UK.

SCORECARD

IS THE UK GOVERNMENT TIGHTENING FOREIGN INVESTMENT REVIEWS? Yes

IS THIS TIGHTENING THE RESULT OF NEW LEGISLATION OR STRICTER ENFORCEMENT OF EXISTING LAWS?
Not clear - it remains to be seen how the UK government will implement its proposals to introduce tighter vetting of foreign acquisitions that raise national security issues in the UK.

The government also has the power to specify other public interest intervention criteria where it sees fit.

Finally, the Industry Act 1975 provides that government intervention is possible when there is a change of control (30% or more) of an "important manufacturing undertaking" resulting in control vesting outside the UK, contrary to UK interests. This has never been invoked.

RECENT DEVELOPMENTS

A NEW REGULATORY REGIME

In October 2017, the UK government confirmed its intention to create a new regulatory regime for foreign investment that raises potential national security issues in the UK. The new proposals go further than the current regime.

Under the short term proposals:

- The government proposes to lower the jurisdictional threshold for review under the UK merger control regime from £70 million to £1 million (financial threshold), and amend the current 25% share of supply test, better allowing the government's review of investments in "(i) the dual-use and military use sector, (ii) parts of the advanced technology sector".

- In particular, this is aimed at broadening the scope of review for transactions beyond defense contractors to capture "enterprises that design or manufacture items or hold related software and technology specified on the

> "Apart from the exercise of a legal right, in practice, whether a bid is successful depends on how the government, investors, the press, unions and others talk about it. It's critical to manage stakeholder interests to get a fair wind behind the offer."
>
> **TIM GEE**
> M&A Partner, Baker McKenzie

UK Military List, UK Dual-Use List, UK Radioactive Source List and EU Dual-Use Lists (i.e. not just those enterprises that currently export these)". Given the breadth of these controls, this could impact a wide range of businesses.

- Review of foreign investments in the technology sector would relate to those enterprises which design, develop, own, create IP etc. related to "multi-purpose computing hardware" or "quantum-based technology", again broadly defined.

The longer term proposals include the following:

- An expanded version of the "call-in power" within the voluntary merger notification regime, to allow the government to scrutinize any transaction where it reasonably believes that national security risks are raised; and/or
- A mandatory notification regime for foreign investment into:
  - a focused set of "essential functions" in key parts of the economy (such as in the civil nuclear, defense, communications, energy and transport sectors);
  - new projects that could reasonably be expected to provide essential functions; and/or
  - specific businesses or assets, potentially capturing businesses which supply critical services or goods to national infrastructure firms.

It is not yet clear which body will review such deals. The UK government is currently consulting on these proposals (the consultation closes in January 2018).

RECENT CASES

In the recent acquisition by Hytera Communications Corporation Limited of Sepura Plc, national security concerns were raised in relation to the protection of sensitive information and technology from unauthorized access. This was the first public interest intervention by the UK government on the grounds of national security in a transaction that did not involve the defense sector.

The Chinese purchaser (Hytera Communications Corporation) was buying Sepura, a UK-based supplier of professional mobile radio systems. Importantly, some of Sepura's radio devices are used by the UK emergency services. In order to avoid an in-depth investigation relating to these national security issues, undertakings were given to provide assurance that sensitive information and technology are protected and to ensure the maintenance of UK capabilities in servicing and maintaining radio devices used by UK emergency services.

The UK's concerns over foreign ownership of UK assets relating to national security are not unique, and similar concerns have been raised in other EU jurisdictions, as well as at EU level.

—

Baker McKenzie helps clients overcome the challenges of competing in the global economy.

We solve complex legal problems across borders and practice areas. Our unique culture, developed over 65 years, enables our 13,000 people to understand local markets and navigate multiple jurisdictions, working together as trusted colleagues and friends to instill confidence in our clients.

www.bakermckenzie.com