Foreign Direct Investment Alert

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EU Locks Down Strategic Assets to Prevent Undervalued Foreign Takeovers During the Pandemic

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The European Commission (EC) on March 25, 2020 issued new guidance on foreign investment screening in response to the COVID-19 emergency[1] (the “Guidance”). The Guidance, which addresses the now 27 EU Member States and relates in particular (but which is “by no means limited”) to health care-related industries, sets out a threefold action plan to tackle COVID-19-related foreign investment risk:

- The EC asks that those Member States which already have national foreign direct investment (FDI) screening mechanisms in place, “make full use” of those mechanisms in order to take into account risks to critical health infrastructures, supply of critical inputs and other critical sectors in Europe.
- Member States that have only limited mechanisms in place, or none at all, are being asked to set up “fully-fledged” screening mechanisms now, and to leverage other available tools in the interim in order to counter critical risks.
- In an unusual request from an EU institution, the Guidance sets out certain restrictions on the free movement of capital, which Member States are asked to deploy alongside more targeted FDI screening tools in order to manage relevant risks.

The Substance of the Guidance

The Guidance is light on prescriptive measures, and focuses instead on enabling action. As such, the bulk of it is made up by the Annex. The Annex provides a recap of the scope of the EU FDI Screening Regulation:[2] The Regulation enables Member States to review foreign investments in all sectors of the economy and irrespective of the size of the target—so long as it is of strategic importance—and to take measures (which need not amount to prevention) to address specific risks to security or public order, including a sell-off of key European businesses and threats linked to a public health emergency. The Guidance notes that critical health infrastructure and inputs are factors that should be taken into consideration when assessing a risk, and reminds Member States (and investors) that an added level of scrutiny applies to “projects or programmes of Union interest,” such as any projects in the health sector receiving Horizon 2020 funding.

Member States are reminded that intervention is also possible outside the ambit of FDI screening mechanisms, for instance, through the imposition of compulsory licenses on medical patents. Furthermore, where necessary and proportionate, Member States may retain "golden shares" that can be used to block or limit certain types of investment. Even investments that do not qualify as FDI, such as portfolio investments even if they do not confer effective influence over a company, may be screened by Member States in compliance with EU provisions on the free movement of capital, for instance where there is an overriding reason to do so. The Guidance emphasizes that "predatory buying" of strategic assets by foreign investors may justify restrictive measures to ensure the security of supply in essential public services, and that intervention may also be justified with respect to acquisitions targeting companies with "valuations on capital markets that are considered well below their true or intrinsic value." Member States may be emboldened in their practices by the fact that the Guidance promotes these examples, which arguably call for significant subjective assessment, indicating that the EC may hold Member State interventions in the current climate to a somewhat lower standard than would be the case otherwise. The final paragraph of the Annex appears to drive this point home: "it needs to be noted that in the analysis of justification and proportionality, restrictions on the movement of capital to and from third countries take place in a different legal context compared to restrictions to intra-EU capital movements […] Consequently, under the Treaty additional grounds of justification may be acceptable in the case of restrictions on transactions involving a third country. The permissible grounds of justification may also be interpreted more broadly."

Background to the Guidance

The new Guidance, which follows a March 13, 2020 Communication from the EC,[3] has been triggered by a combination of factors, but most notably the increased risk of attempts by foreign actors to acquire European providers of critical healthcare products such as medical or protective equipment, and services such as vaccine development. This follows accusations of opportunism levelled by certain EU governments against a reported attempt by the U.S. government to acquire CureVac, a German biotech company with a potentially critical role in finding and developing a COVID-19 vaccine, and to lure its staff, technology and know-how to the United States.

More broadly, European equities have weakened significantly over the course of the spread of the COVID-19 epidemic, which has left companies 'undervalued' and vulnerable to takeovers by those who still possess sufficient financial firepower, including foreign governments. Many European observers also recall with regret that assets with important parts to play in the EU's wider strategies were acquired by foreign powers in the wake of the 2008 financial crisis, and they are keen to avoid a repeat of this.

United Kingdom, Spain, Germany and France

The Guidance trails a wave of tightening FDI screening in Europe, including in the United Kingdom, Germany and France,[4] as well as more targeted responses to COVID-19 crisis, as introduced in Spain on March 17, 2020 and in France, and as currently contemplated in Italy and Germany. Notably, the pandemic-specific restrictions to date do not appear to attempt to re-open "pre-crisis" offers, such as Swiss SIX's offer for Spain's BME for instance, but are rather designed to prevent opportunistic foreign acquisitions of European companies that are currently trading at a discount as a result of collapsing share prices.

What to Expect

Will the current crisis and the European response herald a further tightening of foreign access to European businesses? Current developments could prompt a second look at the FDI Screening Regulation, which expressly covers biotechnology, but that remains months away from being in full effect. Might Member States now see scope for a greater role for the EC in screening foreign investment (the Guidance notes forebodingly (with emphasis added) that "[a]t present, the responsibility for screening FDI rests with Member States"), or in aligning the regime more closely with the reviews carried out in the competition law context, which are often mandatory and suspensory, with the ability to veto an investment or heavily condition it? Moreover, some Member States are likely to take up President Von der Leyen's video call-to-arms to strengthen their existing national screening mechanisms, or to introduce them where none exist at present.

Whatever the future holds, it is clear that the European Union, like the United Kingdom post-Brexit, must carefully balance its protectionist instincts against its desire to remain an open economy and a proponent of frictionless trade. In the short term, the Guidance signals to non-EU investors/acquirers to keep their "hands off" cheap strategic European assets.

[1] Guidance to the Member States concerning foreign direct investment and free movement of capital from third countries, and the protection of Europe's strategic assets, ahead of the application of Regulation (EU) 2019/452 (FDI Screening Regulation).

[2] Regulation (EU) 2019/452 establishing a framework for screening of FDI into the European Union. See also Davina Garrod, Sebastian Casselbrant-Multala, *Akin Gump International Trade Alert: EU Foreign Investment Law In Force from April*, March 6, 2019.

[3] Coordinated economic response to the COVID-19 Outbreak, COM(2020) 112 final

[4] Davina Garrod, Sebastian Casselbrant-Multala, Lennart Garritsen, *Foreign Investment: An overview of EU and national case law*, 16 January 2020, e-Competitions Bulletin Foreign Investment, Art. N° 92104, Davina Garrod, Sebastian Casselbrant-Multala, *Akin Gump International Trade Alert: New U.K. National Security Powers to Call In Investments and Other Transactions*, 26 July 2018.

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