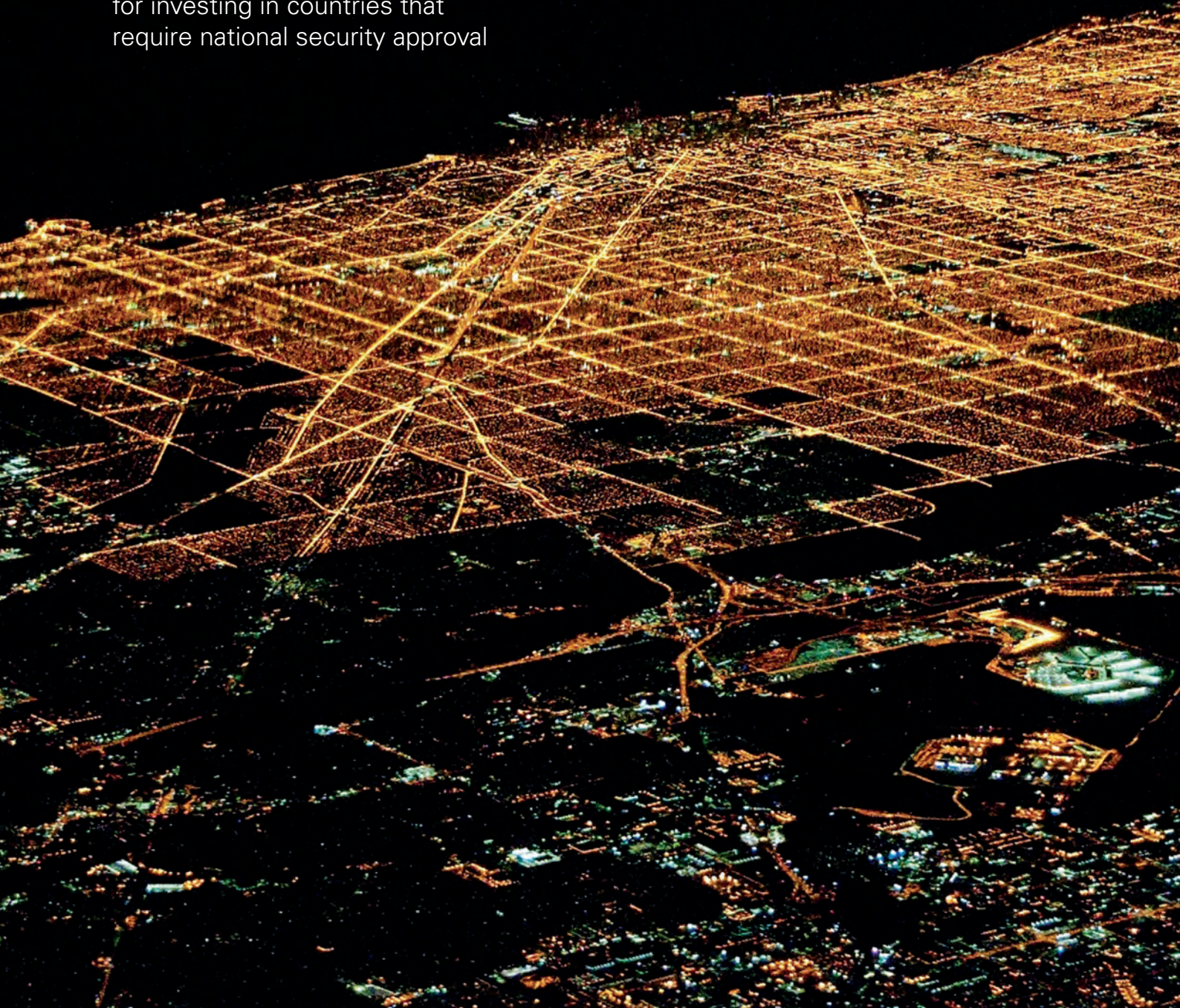
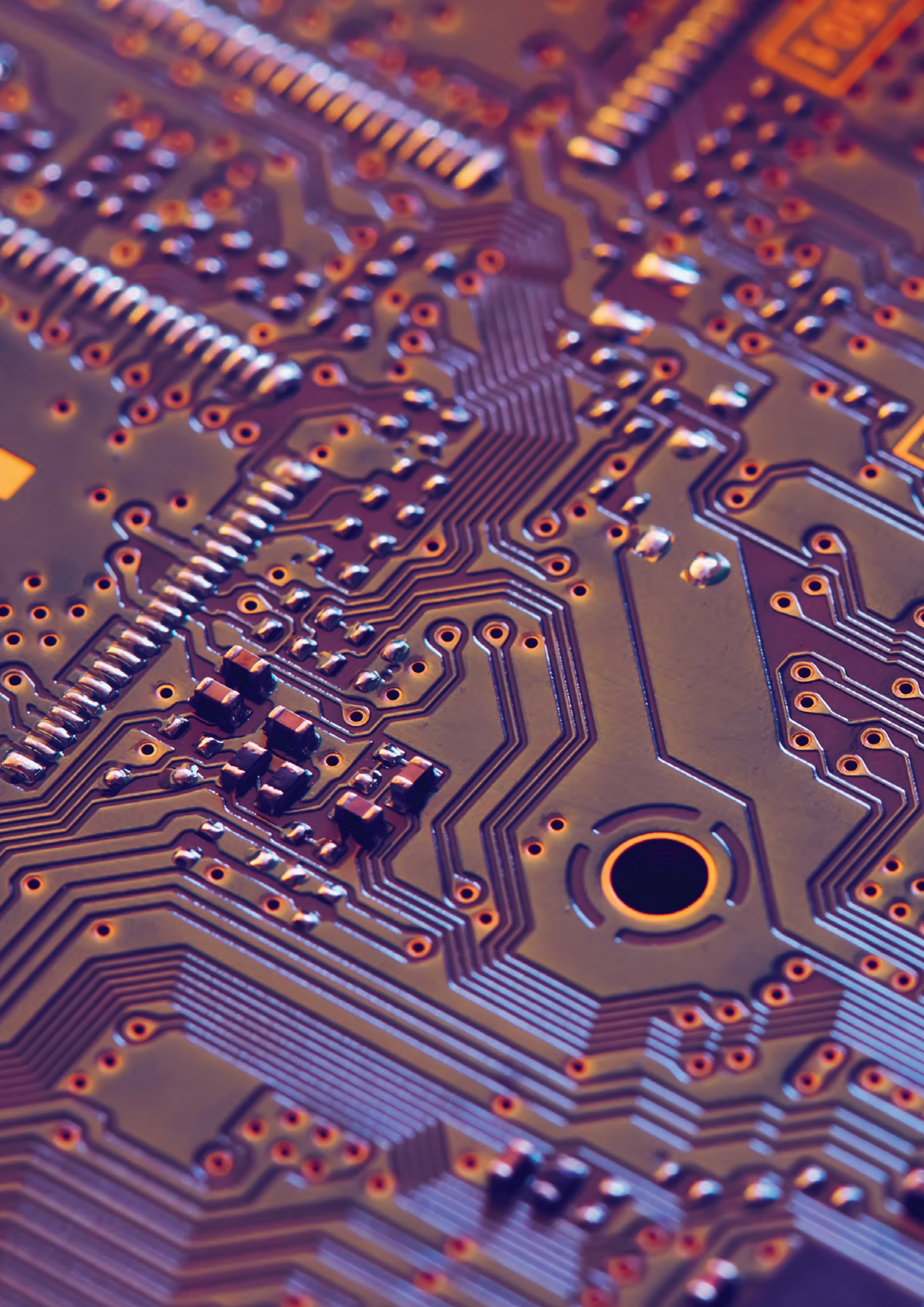


National security reviews 2018: A global perspective

A guide to navigating the rules
for investing in countries that
require national security approval





Navigating national security reviews worldwide



Farhad Jalinous
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As governments in various countries tighten their grip on national security reviews of foreign direct investment, the need for better assessment and calibration of the associated regulatory risk in cross-border transactions is greater than ever before

Nowhere is this trend more evident than in the United States, with the August passage of the Foreign Investment Risk Review Modernization Act (FIRRMA), which expanded the range of transactions that are subject to review by the Committee on Foreign Investment in the United States (CFIUS), and the more recent release of a pilot program under FIRRMA that instituted mandatory declarations for a broad range of transactions and put in place penalties—up to the full value of the transaction—for failure to comply. With CFIUS set to clamp down still further in coming months, CFIUS compliance is rapidly moving to the very top of the due diligence list for cross-border transactions involving US businesses.

The US is far from alone. As you will read in the pages that follow, the European Union, United Kingdom, Germany, France, China and other nations are also incrementally ratcheting up their reviews. In the UK, for instance, the government is proposing radical new legislation to allow it to intervene in cases that raise potential national security concerns. The UK government itself estimates that, under the new law, approximately 50 cases a year may end up with some form of remedy to address such concerns. In France, the new PACTE law is likely to strengthen the sanctions mechanism, extend the list of sectors subject to review and introduce some transparency into the process through annual reporting on a no-name basis of reviewed cases.

The pages that follow offer a common-sense guide to investing in major jurisdictions, a snapshot of recent regulatory changes in each, and guidance on making sound investment decisions in a time fraught with regulatory uncertainty.

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United States

Deals are generally approved, but a new law increases the number and types of deals reviewed

By Farhad Jalinous, Karalyn Mildorf, Keith Schomig and Stacia J. Sowerby

The Committee on Foreign Investment in the United States (CFIUS), which is led by the US Department of the Treasury and made up of US national security and economic agencies, including Defense, State, Justice, Commerce, Energy and Homeland Security, reviews acquisitions of, and investments in, US businesses by foreign persons or businesses.

In August 2018, Congress passed, and President Trump signed, the Foreign Investment Risk Review Modernization Act (FIRRMA), which significantly overhauled the CFIUS process. Although most substantive provisions of FIRRMA will not take effect until new implementing regulations are in place, the key provisions and implications of FIRRMA are discussed where applicable below. CFIUS has also introduced a pilot program mandating short-form notifications for certain transactions involving US companies involved with critical technologies in specified industries.

WHO FILES

The parties to the transaction file a joint voluntary notice that addresses specific information about the investor, the US business and the transaction, and includes attachments such as annual reports, the deal document and information about the target's US government contracts (if any). In most cases, a CFIUS review is ostensibly a voluntary process, but even in some "voluntary" cases it is effectively mandatory; e.g., acquisitions of cleared defense contractors. Moreover, under FIRRMA, the

CFIUS process will no longer be voluntary for transactions involving an investment that results in the acquisition, directly or indirectly, of a "substantial interest" (a term that will be defined in the updated CFIUS regulations) in a US business involved in critical infrastructure, critical technology, or sensitive personal data by a foreign person in which a foreign government has, directly or indirectly, a "substantial interest." FIRRMA also authorizes CFIUS to identify additional transactions that would require mandatory notification, such as those involving critical technology companies. The pilot



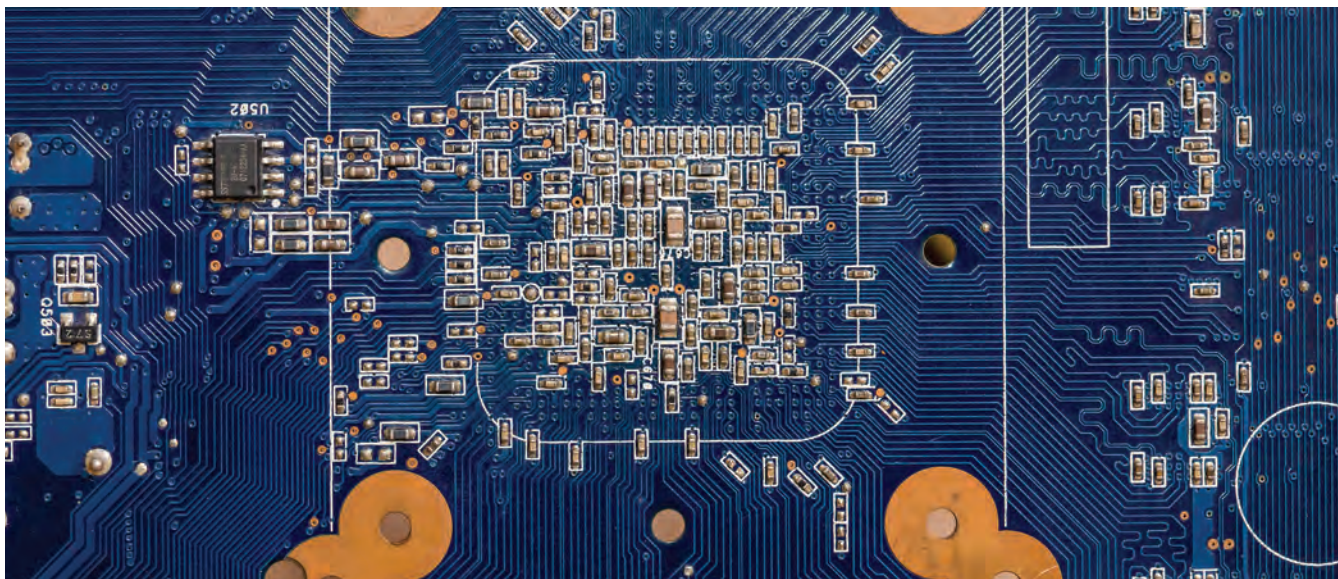
There has been rising sensitivity to China-based transactions, which have continued to increase under President Trump's administration.

CFIUS

In 2018, the Foreign Investment Risk Review Modernization Act (FIRRMA) was enacted, marking the first overhaul of the Committee on Foreign Investment in the United States (CFIUS) statute in more than a decade. FIRRMA was designed to modernize the CFIUS process and close a number of key gaps under the prior law, particularly with respect to Chinese acquisitions.

FIRRMA expands CFIUS's jurisdiction in several ways, most significantly to include purchases or leases of real estate in close proximity to sensitive US government facilities (regardless of whether there is an investment in a US business), as well as non-passive, yet non-controlling acquisitions in US businesses whose activities involve critical technologies, critical infrastructure or sensitive personal data of US citizens. FIRRMA also introduces a "declaration" process for abbreviated notifications that may allow for expedited reviews of certain transactions. FIRRMA also makes declarations mandatory in certain cases—a substantial shift from the current regime, in which CFIUS review is typically a voluntary process. Finally, FIRRMA extends the formal CFIUS timeline by increasing the initial review period to 45 calendar days and authorizing a potential 15-day extension of the 45-day investigation period.

Most of the new law's major changes will not take effect until new implementing regulations are promulgated, which may take as long as 18 months. That said, CFIUS has introduced a pilot program mandating "declaration" filings for certain foreign investments—including non-controlling investments—in companies involved with critical technologies in certain industries.



program has mandated declarations for both controlling and qualifying non-controlling foreign investments in businesses that are involved with critical technologies in certain specified industries. Parties may be subject to penalties up to the value of the transaction if they fail to submit a mandatory declaration.

CFIUS actively looks for transactions of interest that were not notified and will request parties to submit a filing regarding transactions it would like to review. In recent years, CFIUS has reviewed transactions in a wide array of industries.

TYPES OF DEALS REVIEWED

CFIUS currently has jurisdiction to review any transaction that could result in control of a US business by a foreign person, changes in rights that a foreign person has with respect to a US business if that change could result in foreign control of the US business, and any other transaction structured to circumvent the CFIUS process. “Control” is defined—and interpreted by CFIUS—broadly and can include many minority investments. The types of transactions that CFIUS can review are quite varied, including deals structured as stock or asset purchases, debt-to-

equity conversions, foreign-foreign transactions where the target has US assets, private equity investments (in some cases even from US-based companies) and joint ventures where the foreign partner is investing in an acquired or contributed US business.

Under FIRRMA, once new regulations are in effect, CFIUS will also have jurisdiction to review certain real estate transactions (regardless of whether the transaction involves an investment in a US business), and certain non-passive, non-controlling investments involving critical infrastructure, critical technologies, or sensitive personal data (regardless of whether the investment results in control by the foreign investor). As indicated above, CFIUS already has jurisdiction to review non-passive, non-controlling investments in certain cases under the FIRRMA pilot program.

The CFIUS statute does not directly specify what types of industries are relevant to national security. This has given CFIUS substantial leeway to review transactions covering a wide variety of areas, including semiconductors and other technology areas, identity authentication, biometrics, information technology, energy, telecommunications, food safety, financial services, real estate,

cybersecurity and healthcare, as well as industries with a more direct link to national security such as aerospace and defense. External issues unrelated to the structure of the transaction, such as the US business’s location in close proximity to sensitive US government assets, can also pose substantial national security concerns.

Accordingly, it is important to consider CFIUS issues in connection with any transaction involving foreign investment (direct or indirect) in a US business or US real estate with a potential link to national security.

SCOPE OF THE REVIEW

The CFIUS review process is designed to assess the risk profile of the deal from a US national security perspective. CFIUS analyzes the threat posed by the foreign buyer, the vulnerability exposed by the target, and the consequences exposed by the combination of the threat and vulnerability. Based on that risk profile, CFIUS decides if the deal can proceed (with or without mitigation) or whether it needs to be stopped.

Often the analysis is done based on the filing as well as follow-up Q&A. In some cases, the parties will also meet with CFIUS per the parties’ or CFIUS’s request.

TRENDS IN THE REVIEW PROCESS

In recent years, there has been a significant broadening of the foreign investor base represented in CFIUS reviews, with greater activity from emerging markets, such as China, Japan, India and the Middle East.

Notably, there has been rising sensitivity to China-based transactions, which have continued to increase under President Trump's administration. In response, Congress passed FIRRMA, which is intended to close gaps between the transactions that CFIUS is currently able to review and transactions it currently cannot review but that present potential national security concerns. FIRRMA's provisions are particularly aimed at gaps that have been exploited by certain Chinese investment trends. These trends include real estate acquisitions in sensitive areas, minority investments (particularly through private-equity-type structures) that might not be controlling but that nonetheless provide access to sensitive information or technology of the target US business, the increasing use of Chinese joint ventures into which US-origin technology is transferred, and concerns that Chinese deals are being structured to circumvent CFIUS.

To address these types of investments, FIRRMA expands CFIUS's jurisdiction, allowing it to review the following additional types of transactions:

- The purchase or lease by, or a concession to, a foreign person of private or public real estate in the United States that (1) is located within, or will function as part of, an air or maritime port; or (2) is in close proximity to a US military installation or to another facility or property of the US government that is sensitive for reasons relating to national security; could reasonably provide the foreign person the ability to collect intelligence on activities being conducted at such an installation, facility, or property; or could otherwise expose national security activities at such an

installation, facility, or property to the risk of foreign surveillance

- Any "other investment" by a foreign person in any unaffiliated US business that (1) owns, operates, manufactures, supplies, or services "critical infrastructure"; (2) produces, designs, tests, manufactures, fabricates, or develops one or more "critical technologies"; or (3) maintains or collects sensitive personal data of US citizens that may be exploited in a manner that threatens national security
- Any change in the rights that a foreign person has with respect to a US business in which the foreign person has an investment, if that change could result in foreign control of the US business or in an "other investment" involving critical infrastructure, critical technologies, or sensitive data
- Any other transaction, transfer, agreement, or arrangement designed or intended to evade or circumvent the CFIUS process

These provisions are subject to important limitations and caveats. First, the expanded categories of jurisdiction do not go into effect until CFIUS issues new regulations or initiates a pilot program (such as the one already introduced) involving one or more of the categories. Second, FIRRMA requires CFIUS to further limit the term "foreign person" for purposes of the "other investments" and real estate categories, which may exempt certain investors from these expansions. Third, the terms "critical infrastructure" and "critical technologies" must be further defined in forthcoming regulations.

FIRRMA also allows for shorter notifications, called "declarations," which will become a filing option after the FIRRMA-implementing regulations take effect. Declarations may enable some transactions to effectively

receive CFIUS approval based upon an abbreviated notification and in a condensed timeframe. This will also offer an avenue for parties unsure of whether to file to potentially gain clarity without first having to go through a full notice and review. Significantly, while parties will be permitted to start with a declaration (rather than a full notice) in any case, in certain circumstances declarations will be required—meaning that the CFIUS process will no longer be voluntary for such transactions.

In particular, FIRRMA requires a declaration for transactions involving an investment that results in the acquisition, directly or indirectly, of a "substantial interest" in a US business involved in critical infrastructure, critical technology or sensitive data by a foreign person in which a foreign government has, directly or indirectly, a "substantial interest." The term "substantial interest" will be defined in forthcoming CFIUS regulations, and FIRRMA allows the application of this provision to be both narrowed to certain foreign persons and broadened to other types of transactions. Notably, all transactions covered by the initial pilot program—both controlling and non-controlling—are subject to mandatory declarations.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

It is critical for foreign investors to consider CFIUS issues in planning and negotiating transactions, including with respect to allocation of CFIUS-related risk. The range of mitigation requirements that can be imposed is quite wide (based on the risk profile of the deal), and it is important for buyers in particular to have as clear an understanding as possible with respect to what mitigation requirements would be acceptable to them. As a buyer, you do not want to buy an asset and have CFIUS-imposed mitigation prevent you from achieving your objectives for the deal. It is also advisable for investors in potentially sensitive transactions to try to

avoid owing reverse breakup fees should the transaction fail due to CFIUS objections.

REVIEW PROCESS TIMELINE

Typically, the process takes at least four to five months from the time the parties submit the joint voluntary notice and its attachments to CFIUS in draft (called a pre-filing) to completion. Concurrent with a recent surge in CFIUS reviews—2017 well exceeded the previous modern-era record for CFIUS cases in a year and 2018 is at a similar pace—the CFIUS process is often taking longer, sometimes significantly so. CFIUS typically takes about two to four weeks to review and comment on the pre-filing, though in some cases this process can take longer. Thereafter, once the parties incorporate CFIUS's comments and formally file, CFIUS typically takes at least one to two weeks to accept the filing and start a 45-calendar-day review process. At the end of the 45 calendar days, the review is either completed or is taken to the investigation phase (which happens in most filed cases annually).

Investigation can take up to 45 calendar days, and may be extended for one 15-day period in "extraordinary circumstances." Most reviews are completed after the investigation phase. On rare occasions, contentious deals are taken to the president for a decision, who has 15 days to decide. More commonly, typically when CFIUS needs more time to assess a sensitive transaction or parties are still negotiating mitigation terms with CFIUS, CFIUS may encourage the parties to withdraw and resubmit the notice to restart the 45-day review period. In the past couple of years, the number of transactions that have been withdrawn and resubmitted for a second review cycle has increased, though the statutory time period for review and potential investigation was extended under FIRRMA, which may reduce the need for additional review cycles.

2018 UPDATE HIGHLIGHTS

- The number of CFIUS reviews continues to remain high. It is important to incorporate extra time for CFIUS review into deal-planning timelines.
- FIRRMA became law in August, significantly expanding CFIUS's jurisdiction, adding a declaration process, extending the review period, and making other changes to the CFIUS process. The new law is expected to be implemented in large part to capture Chinese investments in ways that were previously beyond CFIUS's reach.
- Under FIRRMA, Chinese deals, particularly those involving sensitive or state-of-the-art technologies, will continue to come under significant scrutiny. Not only Chinese deals are sensitive, however—for example, German-based Infineon abandoned its proposed acquisition of Cree's Wolfspeed business following CFIUS objections. Thus, it is critical to consider potential CFIUS concerns in all cases.
- The same legislation that contained FIRRMA also included the Export Controls Act of 2018, which largely codifies the US Department of Commerce's current administration of its US export control regime but also requires the Department of Commerce to establish export controls on "emerging and foundational technologies" (sensitive technologies not currently captured under the export control regime); conduct an interagency review of license requirements for exports to countries subject to arms embargo; and consider a proposed export's impact to the defense industrial base when reviewing a license application.
- CFIUS introduced the first FIRRMA pilot program in October 2018, which mandates declarations for both controlling and certain non-controlling investments in US critical technology companies engaged in a specified list of industries. Parties should carefully review their transactions to assess whether they are subject to the pilot program requirements.

OUTCOMES

- CFIUS's jurisdiction will be increased to include certain real estate transactions and non-controlling, non-passive investments
- For some investors with foreign-government ownership, a CFIUS declaration will be mandatory in certain cases
- Most deals are still approved and are expected to continue to be approved
- Where CFIUS has national security concerns, it can impose mitigation conditions that can have significant implications on the foreign investor's involvement with the US business
- A relatively small but nevertheless notable number of deals are abandoned while going through the process
- Only the US president can formally stop a deal, which has happened five times in the history of CFIUS—twice during the current administration. More typically, in cases where CFIUS determines there are unresolvable national security concerns, CFIUS will suggest that parties abandon a deal or it will recommend a presidential block, at which point parties usually agree to withdraw from the transaction

Canada

While few deals are challenged in Canada, national security reviews are becoming more common and complex

By Oliver Borgers¹

The Investment Review Division (IRD), which is part of the Ministry of

Innovation, Science and Economic Development Canada (ISED), is the government department responsible for the administration of the Investment Canada Act (ICA), which is the statute that regulates investments in Canadian businesses by non-Canadians.

The IRD interfaces with investors and other parties as part of a preliminary (informal) review of an investment to determine if there are potential national security concerns. Where concerns arise, the IRD will work with the Minister of ISED, in consultation with the Minister of Public Safety and Emergency Preparedness, who will refer investments to the Cabinet (the Canadian Prime Minister and his appointed Ministers, formally known as the Governor in Council), who may order a formal review if the investment could be injurious to Canada's national security. The national security review process is supported by Public Safety Canada, Canada's security and intelligence agencies and other investigative bodies described in the National Security Review of Investments Regulations.

WHO FILES

The ICA is a statute of general application that applies to any acquisition of control² of a Canadian business by a foreign investor. If the relevant financial threshold under the ICA is exceeded, the statute provides for a process of pre-merger

review and approval of foreign investments to determine if they are of "net benefit" to Canada.

If the financial threshold is exceeded, the investor must file an application for review and the transaction must be approved by the relevant Minister. A key element in the application for review is the requirement to set out the investor's plans for the Canadian business, including plans related to employment, participation of Canadians in the business and capital investment. An application for review is a much more detailed document than a notification.

If the financial threshold is not exceeded, the investor has an obligation only to file an administrative notification form, which can be filed up to 30 days after closing.

In either case (filing of an application for review or just a notification), the Canadian government has the jurisdiction for 45 days after receipt of such a filing to order a national security review if there are concerns.

The entry point for national security review screening will usually be the obligatory filing under the ICA (either an application for review if the financial threshold is exceeded, or an administrative notification form if the threshold is not exceeded). The government also has the power to subject non-controlling minority investments to a national security review, although we are not aware of any instances of such a review to date.

TYPES OF DEALS REVIEWED

It is important to keep in mind that the Canadian government has the power to review any transaction (including minority investments) in which there are "reasonable grounds to believe that an investment by a non-Canadian could be injurious to national security." Unlike the "net benefit" review process under the ICA, there is no financial threshold for investments under the ICA's national security review regime.

Further widening the potential scope of the national security review regime is the fact that there is no statutory definition of "injurious to national security." This lack of definition creates wide discretion for the Minister and some uncertainty for foreign investors.

The types of transactions that have been the subject of formal review under the national security lens include those relating to satellite technology, telecommunications, fiber-laser technology and critical infrastructure as well as where a non-Canadian investor proposed to build a factory located in close proximity



Investors subject to Canadian national security reviews have included American companies, as well as investors from emerging markets.



to Canadian Space Agency facilities. Investors subject to Canadian national security reviews have included American companies, as well as investors from emerging markets, but particular scrutiny can be expected for state-owned investors.

SCOPE OF THE REVIEW

The Canadian government recently issued guidelines that shed some light on the circumstances that may draw investors and parties involved in the investment into the realm of a national security review.

A national security review will focus on the nature of the business to be acquired and the parties involved in the transaction (including the potential for third-party influence). In assessing whether an investment poses a national security risk, the Canadian government has indicated that it will consider factors that

focus on the potential effects of the investment on defense, technology and critical infrastructure and supply.

Review can occur before or after closing. Transactions that run the risk of raising national security concerns are encouraged to seek clearance by making any ICA filings well before the proposed time of closing (at least 45 days). The Canadian government may deny the investment, ask for undertakings and/or provide terms or conditions for the investment (similar to mitigation requirements in the United States), or, where the investment has already been made, require divestment.

TRENDS IN THE REVIEW PROCESS

The Canadian government has been steadily increasing its focus on national security (including rejecting mergers due to national security concerns). However, recent

events appear to signal an increased willingness to encourage foreign investment, including the recent issuance of guidelines intended to increase the transparency of national security reviews and the setting aside of the prior federal government's decision requiring a foreign investor to divest its investment in a Canadian business due to national security concerns.

In late 2016, in an unusual move, the new Liberal government consented to setting aside an order made under the previous Conservative government that required O-Net Communications (a high-technology company listed on the Hong Kong Stock Exchange) to divest its investment in ITF Technologies (a specialty fiber components and modules provider in Quebec) on the basis that the investment would be

injurious to national security. Under a fresh national security review, the Liberal government reversed the prior government's decision and approved O-Net's acquisition of ITF Technologies. This development appears consistent with the Liberal government's foreign policy objective to deepen trade relations with China.

By contrast, in 2018 the Canadian government blocked the acquisition of Aecon, a Canadian construction and infrastructure company, by a Chinese state-owned investor after significant public and political opposition. Time will tell whether this move by the government is a sign of an overall policy shift or a unique case.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

Where a transaction gives rise to national security risks, non-Canadian investors should consider filing notice of the transaction with the Minister at least 45 days prior to closing to obtain pre-clearance (assuming the Minister does not order a full national security review). For an investment that does not require notification (i.e., a minority investment), the Canadian government encourages non-Canadian investors to contact the Investment Review Division at the

earliest stage of the development of their investment projects to discuss their investment.

As in other jurisdictions, it is therefore critical for foreign investors to consider Canadian national security review issues in planning and negotiating transactions. In particular, an investor should ensure that it secures a closing condition predicated on obtaining national security clearance in Canada, where appropriate. It may also be appropriate for merging parties to allocate the national security risk.

REVIEW PROCESS TIMELINE

The process can take up to 200 days (or longer with the consent of the investor) from the date the initial notice of the transaction is sent to the Minister of ISED. The Minister has 45 days (which can be extended by up to an additional 45 days) after an application or notification under the ICA has been certified, or after the implementation of a minority investment that does not require notification, to refer an investment to the Governor in Council for an order for national security review. If an order is made, it can take 110 more days (or longer with the consent of the investor) for the review to be completed.

OUTCOMES

- Formal national security reviews have been ordered by the Cabinet 12 times since the national security review process was introduced in March 2009 to March 2017 (the date to which IRD has released statistics)
- Many more transactions have been the subject of informal national security review by the IRD, most often resulting in successful pre-clearance. Only a small fraction of the thousands of notifications and applications for review filed with the IRD have attracted national security scrutiny
- The outcomes of the 12 instances where formal national security reviews were ordered include: The investor was directed to not implement the proposed investment (three cases—one of which was re-reviewed and approved with conditions), the investor was ordered to divest control of the Canadian business (five cases), the investment was authorized with conditions that mitigated the identified national security risks (four cases) and, in one case, the investor withdrew its application prior to a final order being made

2018 UPDATE HIGHLIGHTS

- The Canadian Government continued to robustly apply the national security provisions of the ICA in 2017 – 2018. In 2016 – 2017 (statistics for which were released in 2018), the government issued three divestiture orders and two approvals with conditions to mitigate the potential injury to national security, which reflects greater enforcement action than in any previous year. In May 2018, the government also issued a high-profile block of the CCCI/Aecon transaction, which involved the proposed acquisition of a Canadian construction and infrastructure company by a publicly traded Chinese state-controlled investor. The Minister released a statement noting that “Our government is open to international investment that creates jobs and increases prosperity, but not at the expense of national security,” but did not disclose the security considerations that led to the decision.
- The uptick in enforcement and the government's block of a high-profile transaction suggest that despite its rhetoric about welcoming foreign investment, the government will not hesitate to invoke its enforcement powers where it believes Canada's national security may be threatened. Despite this trend, the vast majority of investments notified or subject to review under the ICA—including acquisitions by state-owned investors and investors from China—are cleared without engaging the national security process.

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² Generally, an acquisition of greater than 50 percent of the equity or voting interests of an entity, though in certain cases an acquisition of greater than one-third of the equity or voting interests of a corporation will be considered an acquisition of control.

European Union

Proposed European foreign direct investment regulation— a first step toward harmonized European investment controls

By Tobias Heinrich, Mark Powell and Orion Berg

Due to the significant increase of foreign direct investment (FDI) into European technology assets over the past 24 months, particularly from the People's Republic of China (PRC), there has been an increased call for the EU to take a more active role in scrutinizing investments.

Responding thereto, Jean-Claude Juncker, President of the European Commission, presented a proposal in September 2017 for an EU Regulation establishing a framework for the screening of foreign direct investments into the EU (Proposal or Draft Regulation). This Proposal aims at striking a balance between maintaining the EU's general openness to FDI and ensuring that the EU's essential interests are not undermined by precisely this openness. The Draft Regulation is currently expected to be adopted ahead of the elections of the European Parliament in May 2019.

KEY OBJECTIVES OF THE PROPOSAL

As of today, only 12 out of 28 Member States have national security review mechanisms in place, differing widely in scope and enforcement. This illustrates the lack of harmonization toward national security reviews within the EU and has cast doubts about the effectiveness of the EU's decentralized and fragmented system of monitoring FDI to respond adequately to new challenges in an increasingly protectionist environment.

Today's European mechanisms differ widely in scope (review of intra- or extra-EU FDI, differing screening thresholds, breadth of

sector coverage), design (pre-authorization vs. ex post screening of FDI) and enforcement. The Draft Regulation falls short of introducing a single EU mechanism but aims to enhance cooperation on FDI screenings between the European Commission and Member States. At the same time, it intends to increase legal certainty and transparency within and among Member States.

PROPOSED SCOPE OF DRAFT REGULATION

The Draft Regulation seeks to establish a general framework for Member States and the European Commission for the review of foreign direct investments into the EU. If Member States decide to opt for legislative investment reviews, those will have to be brought in line with certain minimum standards laid out in the Proposal.

The key entering point to investment reviews will revolve around the criteria of "security and public order." While such terms stem from European law, they are only vaguely defined by the European Court of Justice. The Draft Proposal specifies the criteria by a

non-exhaustive list of sector-specific assets and technologies to be taken into account when conducting a review, including inter alia:

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

The scope of investment reviews laid out in the Draft Regulation reveals conceptual and technical similarities with the latest amendments of the German Foreign Trade and Payments Act (AWV) in 2017 (see chapter on Germany). Additionally, the Proposal takes into account whether the acquirer is "controlled by the government of a third party, including through significant funding." The latter responds to increased volume of investments backed by state-owned enterprises and state-supported funding, in particular from the PRC.

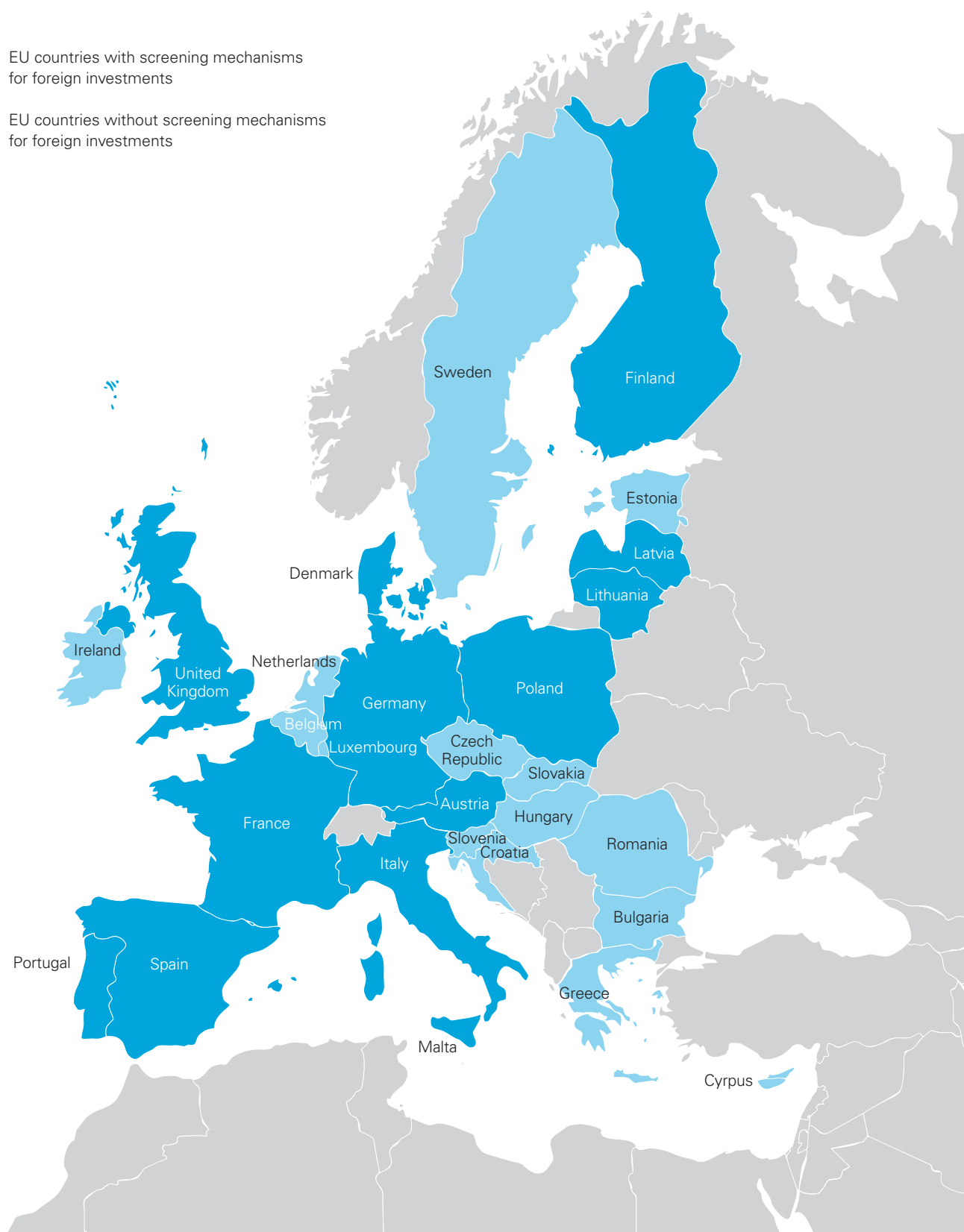
NEW COMPETENCIES FOR THE EUROPEAN COMMISSION

One of the most significant changes to the existing national review mechanisms throughout the EU is the new role of the European Commission as anticipated by the Proposal. The Draft Regulation



Only 12 out of 28 Member States have national security review mechanisms in place, differing widely.

- EU countries with screening mechanisms for foreign investments
- EU countries without screening mechanisms for foreign investments



provides for a cooperation mechanism between the Member States and the Commission by virtue of which the latter shall be authorized to conduct investment reviews in a coordinating and supporting function. Accordingly, Member States will be required to inform the Commission and other Member States of any foreign direct investment undergoing the national review process simultaneously. This raises confidentiality concerns for the parties of a transaction, in particular when considering pre-filings, which the Commission is seeking to actively address.

Going forward, the European Commission may review the respective investment in its own right and issue its opinion to the relevant Member State. Other Member States may also deliver comments to the reviewing Member State, though neither the Commission's opinion nor other Member States' comments will be binding, leaving the ultimate decision on the clearance of a transaction to the reviewing Member State.

Furthermore, the Draft Regulation introduces annual reporting obligations on the part of the Member States with respect to national security reviews on the basis of the information made available to them. This is intended to achieve transparency of national review proceedings through the EU, as most Member States do not provide publicly available information on the domestic review processes or the decisions taken by the relevant authorities.

Should the Commission qualify a transaction as likely to affect projects or programs with significant EU funding (e.g., Galileo, Copernicus, trans-European Networks, etc.), the relevant Member State must "take utmost account of the Commission's opinion and provide an explanation to the Commission in case its opinion is not followed." Yet, even in this context, the ultimate decision remains with the respective Member State.

In summary, the European Commission's role in the review process is generally limited to an advisory responsibility, falling short of the competencies of the Committee on Foreign Investment in the United States (CFIUS). This limited role has been addressed in the current legislative process by the European Economic and Social Committee (EESC) which in its report issued in April 2018 called for an extension of the powers of the Commission. In particular, the EESC proposed to expand the Commission's review competencies to such transactions having a cross-border impact on the whole EU or parts of it.

PROCEDURAL IMPLICATIONS

The implications of the Draft Regulation for existing national review mechanisms are expected to be mostly of a procedural nature. Member States retain the ultimate decision-making power and remain free to opt out of investment reviews entirely.

Given that Member States will be obligated to give the Commission's opinion and other Member States' comments due consideration, the time frames for national review procedures are likely to expand further. This is enhanced by the fact that under the Draft EU-Regulation, Member States will have to inform the Commission and other Member States of the transaction undergoing review within five working days following initiation of the review process. Opinions and comments would need to be submitted within another 25 working days. Should the Commission require additional information, it may request such information from the reviewing Member State and the 25-working-day period will start upon receipt of such information. Should another Member State issue comments before the Commission's opinion, it would trigger a restart of the 25-day-review period, which may significantly reduce predictability of transaction timetables.

LEGISLATIVE PROCESS

A first public consultation on the Proposal took place during the European Parliament's International Trade Committee (INTA) meeting on November 22, 2017. After a number of technical briefings, INTA adopted its report on May 28, 2018 and simultaneously agreed to enter into inter-institutional (trilogue) negotiations as representative of the European Parliament. On June 13, 2018, the EU Member States' Permanent Representatives agreed on the Council's position on the proposed regulation and asked the Presidency to start negotiations with Parliament as soon as possible. A first trilogue meeting took place on July 10, 2018.

The European Parliament's response to the Draft Regulation focuses, inter alia, on the introduction of an Investment Screening Coordination Group as a second institutional coordination body.

The Draft Regulation could be adopted as early as spring 2019 (most likely ahead of the election of the European Parliament at the end of May 2019). It remains open whether the new EU framework would be immediately applicable as proposed in the draft EU Regulation or delayed by a transition period of 18 months, as currently suggested by the EU Council.

OUTLOOK

The new role of the European Commission, possibly an Investment Screening Coordination Group and other Member States, will add another layer of complexity to the review process—a testimony to the increasing significance of security reviews in the field of international M&A. Annual reporting obligations will contribute to reducing the current lack of transparency, and the cooperation mechanism should serve as an important step toward a unified approach throughout the EU. It remains to be seen whether the current proposal is an interim or a more definitive step in the course of harmonizing European investment controls.

Finland

Deals are generally not blocked in Finland

By Janko Lindros

The Finnish government views foreign ownership positively as a catalyst for increasing internationalization and competitiveness. Deals are only restricted when they meet very specific criteria. The objective of the Finnish Act on Monitoring Foreign Ownership (172/2012), also known as the “Monitoring Act,” is to assess foreign investments for their potential impact on national interests. When it is deemed necessary to protect national defense and safeguard public order and security, the government may restrict the transfer of influence to foreigners, foreign organizations and foundations. The Monitoring Act has a special focus on defense industry companies, including dual-use companies.

FILING OBLIGATIONS AND CONSEQUENCES IN THE EVENT OF BREACH

Under the Monitoring Act, a “corporate acquisition” occurs when a foreign owner gains control of at least one tenth, one third or one half of the aggregate number of votes conferred by all shares in a Finnish company—or otherwise secures a holding that confers decision-making authority.

All corporate acquisitions concerning the defense and dual-use sectors require advance approval by Finnish authorities. Deals not related to defense may also be covered by the Monitoring Act if the company being acquired is considered critical for securing vital functions of society. In such cases, investors are not required

to submit an application prior to completing a transaction—but in practice applications are always submitted prior to completion. The government intentionally does not define the phrase “enterprise considered critical for securing vital functions of society” because the definition evolves over time.

For the defense and dual-use sectors, monitoring covers all foreign owners. For enterprises considered critical for securing vital functions of society, monitoring only applies to foreign owners residing or domiciled outside the EU or the European Free Trade Association.

If the Monitoring Act is breached, the transaction can be declared null and void.

REVIEW PROCESS

The review process starts when an investor submits an application to the Ministry of Economic Affairs and Employment. There are no formal requirements for the layout of the application, but the ministry has published instructions for preparing one. It is critical that the

application is made by the potential foreign owner, not a Finnish holding company already set up by the potential new owner. After receipt of the application, the Ministry of Economic Affairs and Employment asks for input from other branches of government.

If the Ministry of Economic Affairs and Employment finds that the transaction may endanger a key national interest, it transfers the matter to the government’s plenary session for resolution. The government’s plenary session then makes the decision about whether to restrict or approve the deal, depending on whether it believes the deal poses a threat to national interest.

However, if the Ministry of Economic Affairs and Employment considers that a transaction does not endanger a key national interest, it approves the transaction. The vast majority of transactions submitted to date have been approved by virtue of this rule.

All applications are urgently processed by the Ministry of Economic Affairs and Employment. The Monitoring Act states that a transaction is deemed to have been approved if the Ministry of Economic Affairs and Employment does not make a decision on an in-depth review within six weeks, or if the application has not been transferred to the Government’s plenary session within three months dating from the day when all necessary materials were received. In practice, the process with the Ministry of Economic Affairs and Employment usually takes six to eight weeks.



The Finnish government views foreign ownership positively as a catalyst for increasing internationalization and competitiveness.

France

New legislation has been proposed to expand the scope of French national security reviews, especially in the technology sector, and to strengthen the powers of French authorities to impose sanctions

By Nathalie Nègre-Eveillard and Orion Berg

The Bureau Multicom 2, which is located within the Ministry of Economy's (MoE) Treasury Department, conducts the review. The process generally involves other relevant ministries and administrations depending on the areas at stake. Since January 2016, a commissioner of strategic information and economic security (attached to the MoE) also assists the Treasury when coordinating inter-ministerial consultations.

WHO FILES

The foreign investor files a mandatory request for prior authorization, which must include detailed information on the investor and its shareholders, the target, the pre- and post-closing structures, financial terms of the transaction and the sensitive activities at stake.

TYPES OF DEALS REVIEWED

Transactions reviewed under the French Monetary and Financial Code (MFC) include:

- Direct or indirect acquisition by a foreign investor of the control of an undertaking whose registered office is established in France
- Acquisition by a foreign investor of all or part of a branch of activity of an undertaking whose registered office is established in France
- For non-EU investors only, acquisition of more than 33.33 percent in the capital or voting rights of an undertaking whose registered office is established in France. French law does not provide for any

materiality threshold—even transactions of modest size can be captured for review.

The review only applies to foreign investments made in sensitive activities listed in the code. For EU-based investors, these activities include defense- and security-related activities and dual-use technologies. For non-EU investors, additional activities are captured (e.g., gambling).

Since May 2014, the scope of activities concerned by national security reviews has been significantly expanded for all foreign investors (whether EU or non-EU) to protect "activities relating to equipment, products or services, including those relating to 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" in seven new sectors: (1) electricity, gas, oil or other source of energy;

(2) water supply; (3) transportation networks and services; (4) electronic communication networks and services; (5) an installation, facility or structure of vital importance; and (6) protection of the public health.

SCOPE OF THE REVIEW

MoE assesses whether the transaction may jeopardize public order, public safety or national security based on the information the investor provided in its submission. Follow-up Q&A and meetings with MoE and other ministries involved are customary. The seller and the target company may also be requested to cooperate with the review.

TRENDS IN THE REVIEW PROCESS

In 2017, following several cross-border deals involving French flagships acquired by foreign investors, French National Assembly created a Parliamentary Enquiry Committee to investigate decisions made by the French State and how French national security interests are protected on such occasions. This puts an increased pressure on the services conducting and coordinating the review process to ensure that they have completed a thorough review of both the activities at stake and the profile and intentions of the foreign investors. Investors, as well as public opinion, also regularly complain about the lack of general public statistics in relation to the French review process (see below potential changes in relation to the PACTE Law). All relevant administrations are



French law does not provide for any materiality threshold—even transactions of modest size can be captured for review.



involved in the review process, and the investor and its counsels, as well as the target company, may be convened to meetings and Q&A sessions in relation to the envisaged transactions. Delineating and retaining strategic activities, jobs and resources in France have also become an increasing strategic concern in the review process, as well as in relation to clearance commitments that may be required on a foreign investor.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

It is critical for foreign investors to anticipate foreign investment control issues ahead of planning and negotiating transactions.

The responsibility for filing lies primarily on the buyer and, if the transaction falls under MFC regulation, prior clearance by MoE should be a condition of the deal. The buyer may also seek a ruling from MoE to confirm whether a contemplated transaction falls within the scope of the MFC.

The seller's cooperation in the preparation and review of the filing is important. If the parties expect that conditions or undertakings will be imposed, the buyer should anticipate discussions with MoE and other interested ministries that may impact the timeline for clearance. In addition, the buyer should consider including a break-up fee or opt-out clause in the transaction documentation to protect its interests if the conditions imposed on the transaction are too burdensome. Preliminary informal contacts with French authorities may also be advisable.

REVIEW PROCESS TIMELINE

MoE must make its decision within two months of its receipt of a complete authorization request.

Longer periods (e.g., three or four months) should be anticipated if MoE requests supplemental information and considers imposing conditions to clear the case.

2018 UPDATE HIGHLIGHTS

The French Government is contemplating amending the French legal framework applicable to national security reviews in the context of the so-called draft PACTE Law. The list of sensitive sectors subject to prior authorization is likely to be expanded to new strategic sectors. The PACTE Law will also amend the sanctions mechanism in case of infringement to the prior approval obligations. The proposed reform aims at giving the French Government a larger palette of possible sanctions it can adapt and leverage depending on the specific situations. Notably, if a transaction has been implemented without prior authorization, the Ministry of Economy (MoE) will have the power to order the investor to amend the transaction or to restore the

previous pre-transaction situation at its own expense. The MoE may also suspend the voting rights of the investor or suspend, restrict or prohibit temporarily the free disposal of all or part of the assets related to the sensitive activities at stake. Similar sanctions will be imposed if an investor did not comply with the clearance conditions imposed by the MoE including divestment of all or part of the sensitive activities at stake. Monetary sanctions in case of infringement to Foreign Investments Control obligations will be increased. The Parliament is also likely to be involved in the process through a new committee in charge of economic security. Finally, the PACTE LAW also provides for the MoE to issue yearly public general statistics (on a no-name basis) in relation to French national security reviews.

OUTCOMES

Once the review is completed, the MoE may:

- ❑ Authorize the transaction without condition (rather rare)
- ❑ Authorize the transaction subject to mitigating conditions/undertakings aimed at ensuring that the transaction will not adversely affect public order, public safety or national security (most of the cases when the MoE decides to review the investment)
- ❑ Refuse to authorize the transaction if adverse effects cannot be remedied (very rare)

Mitigating conditions/undertakings may pertain to the investor's preservation of the continuity of the target's activities and the security of its supply of products or services (for example, maintaining existing contracts with public entities, maintaining R&D capabilities and production in France). They may also include corporate requirements such as ensuring that sensitive activities are carried out by a French legal entity, and/or imposing information-access/governance requirements involving French authorities.

MoE review is a mandatory process. Under the current legal framework, if a transaction subject to review is closed without MoE's prior approval, MoE may order the investor(s) not to proceed with the transaction, to amend the terms of the transaction or to unwind the transaction at their own expense (potentially imposing a financial penalty of up to twice the amount of the original investment). Moreover, contractual agreements in breach of the mandatory process are deemed null and void. Violation of foreign investment rules may also give rise to criminal sanctions of up to five years of imprisonment and a fine of up to twice the amount of the investment. This sanctions legal framework is, however, being reviewed by French Parliament and will likely be modified by the upcoming PACTE LAW that is expected to be adopted during the first quarter of 2019.

Germany

Federal Ministry for Economic Affairs and Energy is enforcing a stricter regime for foreign direct investment reviews

By Tobias Heinrich

Pursuant to the German Foreign Trade and Payments Act (Außenwirtschaftsgesetz; AWG) and the German Foreign Trade and Payments Ordinance (Außenwirtschaftsverordnung; AWW), the German Federal Ministry for Economic Affairs and Energy (Bundesministerium für Wirtschaft und Energie; BMWi) is entitled to review inbound transactions by foreign investors based outside the European Union (EU) or the European Free Trade Association (EFTA). The BMWi may prohibit or restrict a transaction if it poses a threat to the public order or security (öffentliche Ordnung oder Sicherheit) of the Federal Republic of Germany.

In August 2018, the BMWi for the first time threatened to veto a China inbound transaction after the new investment control rules had come into force in July 2017, which brought about significant changes to the landscape of German investment control reviews. In September 2018, the BMWi announced its intention to further tighten the regime for foreign direct investments in Germany with new legislation currently expected to be passed by the end of 2018.

SCOPE OF REVIEW AND TYPES OF DEALS REVIEWED

The AWW distinguishes between a cross-sectoral review for all industries and a sector-specific review that applies only with respect to certain highly sensitive industries. The scope of the latter includes arms and military equipment and encryption technologies as well as other key defense technologies

such as reconnaissance, sensor and protection technologies.

As part of the cross-sectoral review, an intervention by the BMWi requires the investment to pose a threat to public order or security. Such threats are assumed for investments into the following (non-exhaustively listed) technology assets:

- Operators of critical infrastructure that is of particular importance for the functioning of the community
- Companies developing or changing industry-specific software for the operation of critical infrastructure
- Companies entrusted with organizational monitoring measures for telecommunication facilities
- Companies providing cloud computing services above a certain volume
- Companies engaged in the area of telematics infrastructure

The BMWi is entitled to review all acquisitions, whether by way of asset or share deal, by non-EU-based investors. This applies to acquisitions reaching or exceeding directly or indirectly a 25 percent threshold in the target's equity and/or voting rights. The calculation of voting rights will take into account certain undertakings that may be attributed to the ultimate owner, such as an agreement on the joint exercise of voting rights. Asset deals require a comparable test for the respective asset values, whereby 25 percent of the total assets of the acquired business are deemed relevant. In contrast to the sector-specific review, which is applicable to all foreign buyers, the general review process only applies to non-EU/EFTA-based investors.

PROCESS CONSIDERATIONS AND TIMELINE

The completion of the investment review process is by law not required for the consummation of a transaction. However, following the AWW amendments in 2017, the obligation to notify the BMWi of a transaction is no longer limited to a sector-specific review but extends to the cross-sectoral review if the transaction fulfills the criteria mentioned above. Even if the relevant criteria are not fulfilled, foreign investors often decide to initiate the review process by submitting an application to the BMWi for a non-objection certificate (Unbedenklichkeitsbescheinigung) in order to obtain legal certainty.



In September 2018, the BMWi announced its intention to further tighten the regime for foreign direct investments.

As a response to international transactions becoming increasingly complex and sensitive, the review periods were extended significantly as part of the 2017 reform. This leaves the BMWi with considerably more time to perform its review process, which has a significant impact on the overall transaction timetables.

The sector-specific reviews will be completed with a review period of three months (formerly one month). The review process for cross-sectoral reviews is typically initiated by the parties applying for a non-objection certificate. After complete submission of the application, the BMWi has two months to decide whether to issue such certificate or open the formal review procedure. Upon expiration of this period, the non-objection certificate is deemed to have been issued.

The period available to conduct the formal review measures is four months starting upon receipt of all necessary documentation; it is suspended for as long as negotiations on mitigation measures are conducted between the BMWi and the parties involved.

In order to safeguard public order or security, the BMWi may prohibit the transaction or issue “instructions” (taking the form of mitigation measures). Except for acquisitions in sensitive industry sectors, such measures require the approval by the German Federal Government.

RECENT DEALS REVIEWED BY THE BMWI

Since the 2017 amendments to the AWV, 80 transactions have been subject to BMWi investment reviews, more than a third of them directly or indirectly involving a Chinese acquirer.

The first transaction reviewed by the BMWi following the 2017 reform was the acquisition of the German aerospace composite fiber components manufacturer Cotesa by a Chinese consortium.

In August 2018, a Chinese investor dropped its attempt to acquire German toolmaker Leifeld ahead of an expected veto by the German Federal Government, which had indicated its intention to block the transaction but had not yet issued its veto. This decision would have been the first prohibition of a transaction under the revised AWG/AWV.

In July 2018, the German state bank Kreditanstalt für Wiederaufbau–KfW acquired a 20 percent stake in high-voltage grid operator 50Hertz, denying China’s State Grid the acquisition after the transaction had been announced. The government officially confirmed that the acquisition by KfW was aimed at protecting critical infrastructure for energy supply in Germany. The necessity for the intervention of the KfW (according to public sources) arose as the transaction did not fall within the scope of the BMWi’s review competences, given that the stake was below the 25 percent entry threshold.

TRENDS IN THE REVIEW PROCESS

The current market climate is characterized by the BMWi’s substantially increased awareness and persistent efforts toward enhanced scrutiny. Having said that, the overall number of approved transactions (despite recent vetoes) clearly shows that the investment climate in Germany remains liberal for the overall majority of transactions.

The BMWi announced that it is working on further amendments to German investment control laws, which are currently discussed by the relevant governmental bodies. These amendments will include the lowering of the intervention threshold for selected industries. The changes are currently expected to come into force in late 2018.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

Parties to M&A transactions—whether public or private—should carefully consider the risk of foreign investment control procedures as typically being part of the due diligence process. If AWG/AWV rules apply, it may be appropriate that the acquirer initiate discussions with the BMWi even before the signing of an SPA, or, in case of a public deal, the announcement of the transaction. Depending on the timing and the type of offer, the purchase agreement or the public takeover offer and a related business combination agreement will contain corresponding condition precedents and covenants.

In sensitive sector transactions, foreign investments meeting the above-mentioned thresholds must be communicated to the BMWi and should not be closed before the acquisition is approved or deemed to be approved by the BMWi. Any BMWi decision may be challenged before a German court.

OUTCOMES

- Despite recent interventions by the BMWi and the German Federal Government on two Chinese inbound transactions, the overall number of deals approved shows the continuous openness of Germany toward foreign direct investment
- The threshold for a prohibition of a transaction by the BMWi remains high in the current legislative environment, requiring an actual and sufficiently serious danger to public order or security

Italy

Deals are generally not blocked by the Italian government. However, in connection with the clearance process, conditions may be imposed that can have a significant impact on the investment

By Michael Immordino, Ferigo Foscari and Leonardo Graffi

The Italian government, which is led by the President of the Chamber of Ministries, together with any relevant ministry (such as the Defense Ministry, the Ministry of Transport, the Ministry of Communications, etc.), reviews acquisitions of stakes in Italian companies that (i) carry out “strategic activities” in the defense and national security sector and (ii) hold “assets with strategic relevance” in the energy, transport, communication and high-tech sectors.

Italian law provisions on the so-called “golden power” procedure were adopted in March 2012 and were recently amended by a law decree adopted in October 2017 (the Golden Power Law). The amendment provides for new measures to fill in some gaps identified in the application of the existing legislation, as well as to strengthen the existing law. The rules aim to protect Italian companies’ technology and technical, industrial and commercial know-how.

FILING OBLIGATION AND CONSEQUENCES IN THE EVENT OF BREACH

The filing is mandatory and the notification shall be made by the company or by the seller/purchaser, respectively, in relation to (i) any relevant resolutions adopted by the target company, and (ii) any acquisition of interests in a target company by a foreign investor, to the extent that the target company exercises any strategic activity in the defense and national security sector or holds any strategic asset in the energy, transport, communication

and high-tech sectors. Moreover, any purchaser of equity interests in a listed target company active in the defense and national security sector must notify the acquisition if it exceeds the threshold of 2, 3, 5, 10, 20 and 25 percent ownership in the share capital of the listed target company.

The breach of the notification obligation can lead the purchaser to be held liable for a general monetary sanction equal to an amount up to twice the value of the transaction and, in any case, not less than one percent of the turnover realized by the companies involved in the transaction.

TYPES OF DEALS REVIEWED

The Italian national rules specify the industries and sectors having a national interest and the need to be protected from predatory acquisitions by foreign investors. In particular, the Italian government has jurisdiction to review any transaction that (i) in the defense and national security sectors, may harm or constitute a material threat to the Italian government’s essential interests in the defense and national security of Italy; and (ii) in the energy, transportation, communication and high-tech sectors, may harm or constitute a material threat to the fundamental interests of Italy relating to the security and operation of networks and systems, to the continuity of supplies and to the preservation of high-tech know-how. In this context, the types of transactions that the Italian government can review are various in nature and



Since the adoption of the Golden Power Law, the Italian government has exercised its special powers only in relation to 9 golden power procedures, out of more than 50 known filings.

include deals structured as stock or asset purchases, mergers, joint ventures in which the foreign partner is investing in an Italian business, etc., as well as transactions or corporate actions, which may have the effect of changing the target company's ownership structure or purpose, or winding up the target company's business.

SCOPE OF THE REVIEW

Based on the publicly known golden power reviews completed since the adoption of the Italian Golden Power Law (from 2012 onwards), the Italian government mainly focused its attention on transactions leading to: (i) changes in governance and internal policies that could be capable of harming national interests; (ii) transfer of headquarters outside of the Italian territory and total or partial delocalization of the manufacturing activities; and (iii) transfer of know-how outside of Italy and for the benefit of foreign investors, mainly in relation to companies operating in the infrastructure (energy, transportation and TLCs) and high-tech sectors.

The Italian government enjoys broad power to impose restrictions (i.e., the power to veto the resolutions or impose special conditions); however, it appears that the main measures and special conditions that have so far been imposed by the Italian government have included: (i) control measures, in particular with reference to corporate governance and composition of the management bodies of the target companies; (ii) safety measures, such as the approval of safety contingency plans to monitor strategic assets and operations as well as the appointment of a chief safety officer approved by the Italian government; (iii) monitoring measures, such as the establishment of independent committees tasked with the duty to monitor the target's compliance with the above measures imposed by the Italian government; and (iv) other management, organizational and technical measures aimed at preserving the confidentiality of

information and the technological know-how of the target.

TRENDS IN THE REVIEW PROCESS

On the basis of public documentation made available by the Italian Government, as well as of our direct experience in assisting companies with golden power reviews, since the adoption of the Golden Power Law, a number of golden power reviews have been activated and completed before the Italian government. Among these, it appears that the Italian government exercised its special powers only in relation to 9 golden power procedures, out of approximately 50 known filings, in relation to the sectors of defense and national security, transport and communications.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

Foreign investors willing to enter into a transaction in relation to any Italian company operating in the defense or national security sector or holding assets in the energy, transport, communication and high-tech sectors, should evaluate the possibility that a golden power filing is required and should carry out the relevant analysis before entering into any transaction. Moreover, it is crucial for foreign investors to understand and consider the risk that, in the

event that a transaction falls within the scope of the Golden Power Law, it may be possible that the Italian government will veto or impose certain measures or conditions to the completion of the transaction.

REVIEW PROCESS TIMELINE

The filing shall occur within 10 days after the acquisition (typically after signing) or adoption of the relevant resolution, as applicable. Upon receipt of the filing, a standstill period of 15 days begins during which the Italian government carries out the review of the envisaged investment or resolution, and any voting right attached to the acquired interests, are frozen until the date on which the Italian government decides whether to exercise its powers.

In the event that the Italian government requests additional information, the 15-day term may be extended by the Italian government only once and for a maximum period of 10 additional days.

If the Italian government does not exercise its powers before the end of the standstill period (as possibly extended), the transaction or the resolution may be legitimately implemented, as the procedure can be considered completed through a no objection (*silenzio assenso*) of the Italian government after the relevant term has lapsed.

OUTCOMES

- The majority of publicly known notified deals have been approved (i.e., no objection)
- Since the adoption of the Golden Power Law (2012), to date the Italian Government has exercised its powers only to apply specific measures or conditions to the transactions, and to our knowledge, no transaction has been vetoed
- The review process by the Italian Government can last up to a maximum of 25 business days from the filing
- The notification obligation applies only to acquisitions of stakes in Italian companies carrying out "strategic activities" in the defense and national security sector and that hold "assets with strategic relevance" in the energy, transport, communication and high-tech sectors

Russian Federation

New amendments potentially require foreign investors to disclose information about beneficiaries, beneficial owners and controlling persons as part of pre-clearance

By Igor Ostapets and Ksenia Tyunik

The Government Commission on Control Over Foreign Investments in the Russian Federation (the Government Commission), which was established by the Russian government in 2008, is responsible for the review of applications. The Government Commission is headed by the Chairman of the Russian government and composed of the heads of certain ministries and other government bodies.

Although the final decision on the application is made by the Government Commission, all the preparatory work (i.e., reviewing an application's completeness, liaising with relevant government bodies) is done by the Federal Antimonopoly Service (FAS). FAS, among other things, performs a preliminary review of the application and prepares materials for a further assessment by the Government Commission.

WHO FILES

An acquirer must file if the proposed acquisition would result in the acquirer's control over an entity engaged in activities of "strategic importance" to Russian national defense and security (a Strategic Entity). The acquirer is required to obtain the consent of the Government Commission prior to the acquisition of control over a Strategic Entity; otherwise, the respective transaction is void.

To apply for the consent, the acquirer must submit an application to FAS with attachments, which include, among other things,

corporate charter documents of the acquirer and the target, information on their groups' structures (including the whole chain of control over both the acquirer and the target), transaction documents and a business plan for the development of the target post-closing.

TYPES OF DEALS REVIEWED

The Government Commission reviews transactions that result in acquisition of control over Strategic Entities. Foreign investors must also obtain the Government Commission's consent for certain transactions involving the acquisition of a Strategic Entity's property.

The list of activities of "strategic importance" currently comprises 46 activities that, if engaged in by the target, cause the target to be considered a Strategic Entity. The 46 activities encompass, among others, areas related to natural resources, defense, media and monopolies. The activities include not only those directly related to the state defense and security (e.g., operations with

nuclear materials, production of weapons and military machines), but also certain other indirectly related activities (e.g., TV and radio broadcasting over certain territories, extraction of water bioresources and publishing activities).

The criteria for determining control are rather wide and are lower (25 percent) for a target that is involved in the exploration of "subsoil blocks of federal importance" (e.g., oil fields with a certain size of reserves, uranium mines, and subsoil blocks subject to exploration within a defense and security zone).

Foreign public investors (i.e., foreign investors controlled by foreign states or international organizations) are prohibited from obtaining control over Strategic Entities (for Strategic Entities involved in exploration of subsoil blocks of federal importance, that would mean the limit is 25 percent) or acquire more than 25 percent of a Strategic Entity's property, and must obtain consent of the Government Commission for acquisitions of the reduced stakes in Strategic Entities. In 2017, the special, stricter regime established for foreign public investors was extended to "off-shore companies" (entities registered in jurisdictions from a list approved by the Ministry of Finance, including among others the UAE, Jersey, BVI and Bermuda). Amendments adopted in June 2018 replaced the category of an "off-shore company" with the category of a "non-disclosing investor" (i.e., an investor refusing to disclose to FAS the information about its



Of 229 applications reviewed in the last ten years, the Government Commission approved 216.



beneficiaries, beneficial owners and controlling persons). Non-disclosing investors from any jurisdiction are subject to a more restrictive regime similar to the regime applicable to foreign public investors. In the absence of any clarifications regarding the application of the amendments, the new provisions may be interpreted broadly, meaning that a foreign investor planning to enter into a transaction in respect of the Strategic Entity would likely need to make a prior disclosure of its controlling entities' beneficiaries and beneficial owners in order to avoid being treated as a "non-disclosing" investor.

Certain transactions in respect of Strategic Entities or their property are exempt from the necessity to obtain the Government

Commission's approval (e.g., transactions in which the acquirer is ultimately controlled by the Russian Federation, constituent entities of the Russian Federation or a Russian citizen who is a Russian tax resident and does not have any other citizenship, as well as certain "intra-group" transactions).

Amendments to Russia's foreign investment laws introduced in 2017 gave the Chairman of the Government Commission the right to decide that prior approval is required with respect to any transaction by any foreign investor with regard to any Russian company, if this is needed for the purpose of ensuring national defense and state security. Upon receipt of such a decision from the Government Commission, FAS will notify the

foreign investor about the need to receive approval for a prospective transaction. Any transaction made in breach of this requirement is void. What transactions could potentially fall under the requirements of this amendment are yet to be determined in practice. According to FAS clarifications expressed in media, in practice this rule will apply to very exclusive cases only.

SCOPE OF THE REVIEW

Generally, a review of the application assesses the transaction's impact on state defense and security.

FAS initially requests opinions of the Ministry of Defense and the Federal Security Service as to whether the transaction poses any threat to the Russian defense and security. Additionally, if the

target has a license for dealing with information constituting state secrecy, FAS requests information from the Interagency Committee for the State Secrecy Protection on the existence of an international treaty allowing a foreign investor to access information constituting state secrecy.

Russian law does not provide for more details on the review's scope or the criteria on which the transaction under review is assessed.

TRENDS IN THE REVIEW PROCESS

The year 2018 was the anniversary year for the Russian Strategic Investments Law, which was adopted in 2008. During these 10 years FAS considered 516 applications by foreign investors, of which 229 were sent for review by the Government Commission (other applications either did not require approval and were returned to applicants, or were withdrawn by applicants themselves). Of 229 applications reviewed, the Government Commission approved 216. The top-three attractive spheres of investments were fuel and energy complex, sea ports and airports.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

At the early stage of a transaction, a foreign investor should analyze whether the target company qualifies as a Strategic Entity and whether the planned transaction triggers the necessity of the Government Commission's consent in light of the recent amendments. It is also advisable to analyze whether such consent would be needed in case the acquirer is qualified as a "non-disclosing" investor. This will allow the investor to start filing preparations and then file its application sufficiently in advance to manage the filing's impact on the timing of the transaction.

If the planned transaction does not require prior consent but such would be needed if the acquirer is qualified as a "non-disclosing" investor, it is necessary to disclose

to FAS in advance information on the acquirer's beneficiaries, beneficial owners and controlling persons.

REVIEW PROCESS TIMELINE

The statutory period for reviewing the application is three months from the date of its acceptance for review. The Government Commission can extend the review period for an additional three months.

2018 UPDATE HIGHLIGHTS

- Russia's foreign investment laws were again amended in 2018
- The most significant amendment is a replacement of the category of an "offshore company" with the category of a "non-disclosing investor" (i.e., investor not disclosing the information about its beneficiaries, beneficial owners and controlling persons)
- Noteworthy, amendments do not address the information disclosure requirements to offshore companies only, which means that, literally interpreted, they apply to all categories of foreign investors. Foreign investors deemed as "non-disclosing" investors will be subject to special, stricter rules applicable to foreign public investors. However, amendments do not specify when and how a foreign investor

must be making a relevant disclosure with the FAS. Thus, in the absence of any clarifications regarding the application of the amendments, these provisions may be interpreted broadly, meaning that a foreign investor planning to enter into a transaction in respect of the Strategic Entity would likely need to make a prior disclosure of its controlling entities' beneficiaries and beneficial owners in order to avoid being treated as "non-disclosing" investor

- Amendments clarified the application of criterion of the "aggregate control" over Russian Strategic Entities, which exists where several unrelated foreign public investors, and from June 2018 also "non-disclosing" investors, collectively own more than 50 percent of shares in the Strategic Entity. Pursuant to the amendments, when assessing existence of the "aggregate control" over Strategic Entities that are public companies for the purposes of the Russian Tax Code, the shares belonging to "non-disclosing" investors should not be counted. It is unclear whether this principle will also apply to acquirers (foreign investors) that are public companies for the purposes of the Russian Tax Code

OUTCOMES

- Most transactions submitted to the Government Commission for review are approved. Such approval contains the term within which the respective acquisition needs to be completed. The acquirer can subsequently apply to the Government Commission with a substantiated request to extend this term, if necessary
- The Government Commission can approve the transaction subject to certain obligations imposed on the foreign investor. Until recently, the list of such obligations was exhaustive and established by law. Amendments of 2016 allowed the Government Commission to impose any type of obligation on the foreign investor. Those obligations may include the obligation to invest certain amounts of funds into activities of the Strategic Entity, or to process bioresources or natural resources extracted by the Strategic Entity on Russian territory
- The Government Commission can reject the application for approval of the acquisition

United Kingdom

National security interventions have, with one exception, involved defense considerations

By Marc Israel

Over the past year, there have been a number of important changes (actual and proposed) to legislation permitting intervention by the UK Government in transactions that may raise national security concerns. Unlike many other jurisdictions, acquisitions in the UK in potentially sensitive industries do not, as a matter of course, require parties to seek approval from a regulator or the Government.

Following a Government consultation designed to “strengthen powers for scrutinizing the national security implications of particular types of investment” the notification regime remains voluntary. However, a number of changes have been implemented to strengthen the Government’s powers and allow for intervention in a wider range of cases.

SHORT-TERM CHANGES

The Government adopted some changes in June 2018, and is also proposing more wide-reaching changes that will require a new Act of Parliament. The changes introduced in June 2018 were designed to fill a gap and cover those cases with the greatest potential to raise national security concerns but which were not caught by existing legislation.

These short-term changes amended the Enterprise Act 2002 to reduce the thresholds at which interventions could be made in cases involving a target active in one of three areas: the development or production of military or dual-use

goods; the design and maintenance of computing hardware; and the development or production of quantum technology.

The Government can now intervene in an acquisition in any of these areas if the annual UK turnover of the target is £1 million or more (reduced from £70 million, which remains the threshold for all other cases), or if the target alone accounts for 25 percent or more of purchases or sales of any goods or services in the UK. Previously, the parties had to overlap such that there was an increment leading to a combined share of supply of 25 percent or more. This requirement no longer exists for cases in the three identified sectors, and a deal can be caught even if there is no overlap with the purchaser.

The Government anticipates between five and 29 additional cases per year will be caught by the amendments that came into force in June 2018.

LONG-TERM CHANGES

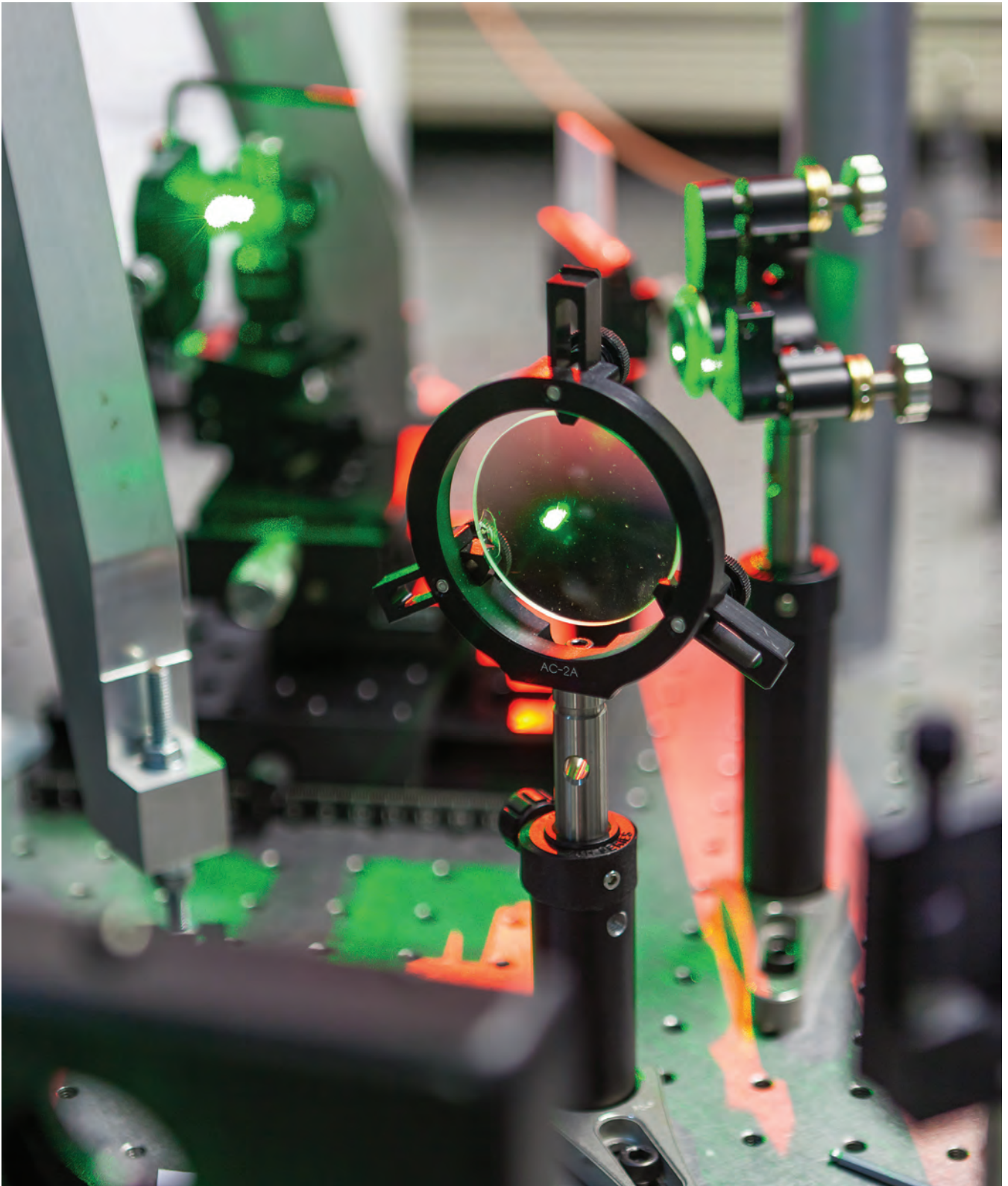
The Government’s long-term objective is to more comprehensively reform its powers of scrutiny over investments that may pose a risk to national security. The intention is to implement this regime with a new piece of primary legislation.

Under the proposed changes, notification will remain voluntary but parties will be encouraged to notify their transaction. As with the UK’s general merger regime, transactions that are not notified may be subsequently investigated and remedies imposed if found to be problematic. The Government expects approximately 200 notifications a year under the new national security regime and that approximately half of these will progress to a full assessment. Of those, the Government estimates that 50 will result in a remedy of some sort, which could vary from implementing some ring-fencing (e.g., of individuals and/or information) to outright prohibition.

Where parties choose not to notify, the Government may still decide to “call in” transactions that result in a “trigger event.” It is proposed that these trigger events will include the acquisition of more than 25 percent of an entity’s shares or votes, significant influence or control over an entity, or further acquisitions of significant influence or control over an entity beyond these thresholds. Acquisitions of assets will also be covered, which is not always the case under the existing rules. The timescale for post-closing intervention in national



The changes introduced in June 2018 were designed to fill a gap and cover those cases with the greatest potential to raise national security concerns but which were not caught by existing legislation.



security cases will be increased to six months after the details of the transaction are in the public domain (the current time limit is four months).

The Government has indicated that it will consider three factors when determining whether a trigger event could lead to a national security risk: “target risk,” whereby the entity or asset in question could be used to undermine national security (i.e., where the nature of the target’s business could pose a potential risk); “trigger event risk,” whereby the acquisition itself gives someone the means to undermine national security (e.g., by affording greater opportunity for disruptive actions or espionage); and “acquirer risk,” where the acquirer itself has the potential to use its control over the target to undermine national security (e.g., where acquisitions are carried out by entities controlled by hostile states or other hostile parties).

The new legislation will provide that all national security considerations be assessed by the Government. Therefore the existing role of the Competition & Markets Authority (CMA)—the UK’s main antitrust agency—to investigate and report to the Government when an intervention is made will be removed. The proposed legislation will also introduce civil and criminal sanctions to deal with non-compliance with any remedies that might ultimately be imposed.

The Government is expected to publish draft legislation in 2019, following its assessment of comments received as part of the current consultation process. As a degree of uncertainty still surrounds details of the proposed new regime and the fact that any new legislation is unlikely to take effect until 2020 at the earliest, the remainder of this article focuses on the existing law.

WHO FILES

As there are currently no specific requirements relating to deals that may raise potential national security

issues, strictly speaking no person needs to file an application. Rather, if the UK Government considers that a deal raises national security issues, the Secretary of State (SoS) may issue an “intervention notice.”

The procedures for the SoS to issue an intervention notice, and—if considered appropriate—ultimately block a deal, are set out in the Enterprise Act. If an intervention notice is served, then the acquirer (and others as appropriate) will be required to provide information.

TYPES OF DEALS REVIEWED

The Enterprise Act currently allows the SoS to intervene when specified public interest considerations arise. In addition to national security, the other specified public interest considerations relate to media plurality, quality and standards, and the stability of the UK’s financial system. These powers have been bolstered by the June 2018 amendments mentioned above if the target is active in military or dual use goods, computing hardware or quantum technologies.

Prior to the June 2018 amendments, there was no guidance as to what industries were relevant to national security, although in all but one case national security intervention notices involved defense considerations. The lowering of thresholds for transactions involving targets active in computing hardware and quantum technology in June 2018 indicates that there is potential going forward for a greater number of non-defense-related transactions to be scrutinized on national security grounds.

The first Government intervention under the new thresholds was in the aerospace sector, with a target active in the manufacture of dual-use goods. That case—the proposed acquisition of Northern Aerospace Limited by Gardner Aerospace Holdings Limited, a Chinese company—was ultimately cleared by the Government (although the intervention caused the deal to be abandoned).

In cases to date, the Ministry of Defence on several occasions raised concerns about the maintenance of strategic UK capabilities and the protection of classified information, including when the acquirers have been from the US or other NATO allies. In these cases, the deals have been approved following undertakings provided by the acquirer to address the concerns, often involving the ring-fencing of sensitive information.

SCOPE OF THE REVIEW

When an intervention notice on national security grounds is issued, the CMA must investigate and report to the SoS—but, as noted above, the legislative proposal is to remove the CMA from all national security reviews. Under the current system the CMA will consult on the national security issues and its report will summarize any representations received on the matters specified in the SoS’s intervention notice and, where relevant, will also deal with any competition issues.

The SoS will consider the CMA’s report and decide whether the transaction should be subject to a more in-depth “Phase 2” review by the CMA, or whether to accept any undertakings the acquirer may have offered to address public interest concerns, or indeed—which has never happened to date—whether the public interest concerns are not warranted or do not require any remedial action.

If there is an in-depth review by the CMA, it is required to report whether the transaction operates or may be expected to operate against the public interest, and make recommendations as to the action the SoS or others should take to remedy any adverse effects. The SoS will make the final decision on the public interest issues and any remedial steps to address the public interest issues.

TRENDS IN THE REVIEW PROCESS

The specific focus in the recent reforms on military and dual-use

technology, quantum technology and computing hardware reflects the fact that national security risks are increasingly likely to arise in the technological and cyber spheres. As general concerns about cybersecurity and control of critical infrastructure networks become more commonplace, it would not be surprising to see more SoS interventions on national security grounds.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

Potential issues should be considered as early in the planning process as possible, and increasingly in any case—not just defense-related deals—that might be considered to touch on national security. State-owned acquirers, or those with material links to (or financing by) state-owned enterprises, should be particularly well prepared, and consider what undertakings they might be prepared to give, if concerns are raised.

To date, such undertakings have tended to relate to ensuring the protection of classified information and ensuring UK capabilities. Early engagement with the relevant Government departments would also be sensible, especially if an auction process is likely, because the target will want to ensure that the acquirer is able to complete any proposed deal. The collapse of the Gardner/Northern deal may have been due, in part, to inadequate planning and preparation on the potential national security issues.

REVIEW PROCESS TIMELINE

Under the current regime, the CMA typically reports to the SoS within four to six weeks of the intervention notice, with the SoS's decision following shortly thereafter. If the SoS decides the CMA should conduct a Phase 2 investigation, it will take up to a further 24 weeks (followed by the time for the SoS to reach a final decision).

2018 UPDATE HIGHLIGHTS

- The thresholds at which Government interventions can be made have been lowered in cases involving targets active in one of three areas: the development or production of military or dual-use goods; the design and maintenance of computing hardware; and the development or production of quantum technology
 - The Government can now intervene in an acquisition in any of these areas if the annual UK turnover of the target is £1 million or more (reduced from £70 million, which remains the threshold for all other cases), or if the target alone accounts for 25 percent or more of purchases or sales of any goods or services in the UK. Previously, the parties had to overlap such that there was an increment in their combined share of supply
- resulting in a share of 25 percent or more. This requirement no longer exists for cases in the three identified sectors
- Under the lower thresholds in these three specific sectors, the UK Government anticipates an additional 5 to 29 mergers will be captured annually by the new rules
 - More wide-reaching changes to the national security landscape are planned. New legislation is proposed, which will cover a wider range of transactions that may pose a risk to national security (including acquisitions of assets). The revised regime will remain voluntary, meaning that there will be no obligation to notify deals that may affect national security. However, non-notified deals will be susceptible to review for up to six months after details become public

OUTCOMES

- No deal has been blocked by the SoS on national security grounds
- All national security cases to date have resulted in behavioral remedies (e.g., ring-fencing information and ensuring strict controls are in place) in lieu of a detailed Phase 2 investigation. No divestments have been required
- Intervention on national security grounds is no longer limited only to defense-related transactions
- The radical changes proposed by the Government to the rules for reviewing deals potentially affecting national security are likely to have a material impact on M&A in the future

Australia

Australia requires a wide variety of investments by foreign businesses to be reviewed and approved before completion

By John Tivey, Barnaby Matthews and Kevin Chen

The decision to approve or deny a foreign investment application is ultimately made by the Treasurer of Australia, based on an assessment of whether the investment would be contrary to the national interest. When making its decision, the Treasurer is advised by the Foreign Investment Review Board (FIRB), which examines foreign investment proposals and advises on the national interest implications. Australia's foreign investment policy framework comprises the Foreign Acquisitions and Takeovers Act 1975 ("the Act"), the Act's related regulations, Australia's Foreign Investment Policy ("the Policy") and a number of guidance notes.

WHO FILES

A foreign person or entity making an acquisition that requires approval under the Act must apply to FIRB for a notification that the Treasurer has no objection to the acquisition ("FIRB approval") before completion of the acquisition, and any agreement to make the acquisition must be subject to receiving FIRB approval.

An application includes a filing fee that varies according to the type of deal and the deal value.

TYPES OF DEALS REVIEWED

FIRB approval is required for a range of acquisitions by foreign persons, including:

- A "substantial interest" in an **Australian entity**: An acquisition of an interest of 20 percent or more in an Australian

entity valued at more than AUD 261 million (approximately US\$189.5 million)

- **Australian land and land-rich entities**: Various acquisitions of interests in Australian land are regulated with varying monetary thresholds, including in respect of residential land, vacant commercial land, developed commercial land and an entity where the value of its interests in Australian land exceeds 50 percent of the value of its total assets
- **Agricultural land and agribusinesses**: Acquisitions of interests in agricultural land and agribusinesses are regulated separately in the Act. In addition, a register of foreign ownership of agricultural land is maintained by the Australian taxation authority
- Certain types of investors receive differing treatment for their deals:
- Free trade agreement investors: Consistent with Australia's

free trade agreement (FTA) commitments, higher monetary thresholds apply to certain acquisitions made by investors from Chile, Japan, Korea, China, Singapore, New Zealand and the United States. For example, an acquisition of an Australian entity by an FTA country investor will only require FIRB approval if the entity is valued at more than AUD 1.134 billion (approximately US\$823 million), unless the investment relates to a "sensitive business" such as media, telecommunications, transport, defense and military-related industries (to which a lower threshold applies) or the investor is a foreign government investor

- **Foreign government investors**: Stricter rules apply to foreign government investors which can include domestic or offshore entities where a foreign government and its associates hold a direct or upstream interest of 20 percent or more, or foreign governments of more than one foreign country and their associates hold an aggregate interest of 40 percent or more. In general, foreign government investors must obtain FIRB approval before acquiring a direct interest (generally, at least a 10 percent holding or the ability to influence, participate in or control) in any Australian asset or entity regardless of the monetary thresholds for FIRB approval, starting a new business or acquiring mining, production or exploration interests



FIRB is more closely scrutinizing investments in sensitive sectors (especially power) and is more likely to impose conditions on such investments to increase government oversight.



SCOPE OF THE REVIEW

The Treasurer may prohibit an investment if he or she believes it would be contrary to the national interest. In making this decision, the Treasurer will broadly consider:

- The impact on national security (with advice from the Critical Infrastructure Centre

on national security risks to critical infrastructure)

- The impact on competition
- The effects of other Australian government laws and policies (including tax and revenue laws)
- The impact on the economy and the community
- The character of the investor

TRENDS IN THE REVIEW PROCESS

Historically, there have been few rejections by the Treasurer on the grounds of national interest. However, there have been some significant investment proposals that have been rejected on national security grounds, including the blocking of the New South Wales government's proposed sale of

its electricity network Ausgrid to Chinese and Hong Kong investors in 2016. In 2016 – 2017, only two non-residential land applications were formally rejected (out of a total of 1,159 applications). These rejections both related to the Ausgrid acquisition.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

Foreign persons should file an application in advance of any transaction or make the transaction conditional on FIRB approval, and a transaction should not proceed to completion until the Treasurer advises on the outcome of its review. For a more sensitive application (e.g., a transaction involving the power, ports, water, telecommunications banking or media sectors), foreign investors should consider taking up the government's invitation in the Policy to engage with FIRB before filing an application for a significant investment.

These discussions may help foreign investors understand national interest concerns the government may hold about a particular proposal and the conditions the Treasurer may be considering imposing on the proposal should it be approved.

These discussions can also help with structuring a transaction in order to reduce the likelihood of rejection. Such discussions should be held at an early stage in order to provide enough time to satisfy all FIRB queries. Where there is a competitive bid process for the acquisition, a foreign investor that does not actively engage with FIRB early in the bidding process may be placed at a competitive disadvantage to other bidders who do. Foreign investors should be prepared to discuss in detail any conditions and undertakings that may be requested by FIRB, especially for acquisitions that are likely to attract greater political or media scrutiny.

REVIEW PROCESS TIMELINE

Under the Act, the Treasurer has 30 days to consider an application and make a decision. The time frame for making a decision will not start until the correct application fee has been paid in full. If the Treasurer requests further information from the investor, the 30-day time period will be on hold until the request has been satisfied. The Treasurer may also extend this period by up to 90 days by publishing an interim order. An interim order may be made to allow further time to consider the exercise of the Treasurer's powers. Investors can also voluntarily extend the period by providing written consent.

2018 UPDATE HIGHLIGHTS

– Open and transparent sale process for agricultural land:

From early 2018, it has been a requirement that acquisitions of agricultural land have been offered for sale publicly and marketed widely for a minimum of 30 days (so as to ensure Australians have sufficient opportunity to invest). Various exceptions apply, including to leasehold interests for wind and solar farms, internal reorganizations and acquirers with a substantial Australian ownership.

– Major electricity assets:

The Treasurer has flagged that acquisitions of major electricity assets would require conditions or ownership restrictions to address national security risks.

– National security review of Australian critical infrastructure assets:

In January 2017, the Attorney General's Department established the Critical Infrastructure Centre (CIC) to support the Australian government's capacity to manage the national security risks of espionage, sabotage and coercion. The CIC administers the *Security of Critical Infrastructure Act 2018* and the *Telecommunications and Other Legislation Amendment Act 2017* to gather information from owners and operators of critical infrastructure in the sensitive sectors of electricity, water, ports and gas (and from carriers and carriage services providers in the telecommunications sector). The CIC then uses this information, together with expertise from across the Australian government, to provide coordinated advice to FIRB on national security risks to critical infrastructure as part of the foreign investment review process.

OUTCOMES

- Generally, the Treasurer approves the vast majority of applications
- However, FIRB has been increasingly willing to use conditions and undertakings as a mechanism to increase the government's oversight of more complex or sensitive investments. Undertakings required from FIRB may include matters relating to governance, location of senior management, listing requirements, market competition and pricing of goods and services (e.g., that all off-take arrangements must be on arm's-length terms) and other industry-specific matters. FIRB has also issued a set of standard tax conditions that apply to those foreign investments that pose a risk to Australia's revenue and make clear the requirements and expectations for investors
- The Treasurer has wide divestiture powers and criminal and civil penalties can apply for serious breaches of Australia's foreign investment laws

China

China is attempting to implement a more structured and comprehensive system to keep a closer eye on economic deals that might have security implications

By Z. Alex Zhang

The ministerial review panel established by China's Ministry of Commerce (MOFCOM) pursuant to a rule issued by the State Council in 2011 (the 2011 Rule) is responsible for conducting national security reviews of foreign investments in domestic enterprises.

In addition to the 2011 Rule, China is in the process of implementing a comprehensive set of rules and regulations governing national security reviews for foreign investments. On July 1, 2015, China promulgated the new PRC National Security Law (the NSL), which is China's most comprehensive national security legislation to date. However, the NSL's main provisions do not detail how these security measures will be implemented by the relevant agencies and local authorities.

As such, the NSL's full impact on individuals and corporations in the private sector will remain unclear until relevant implementation measures are issued.

WHO FILES

According to the 2011 Rule, MOFCOM reviews foreign-investment transactions following voluntary filings by the parties to the transaction, referrals from other governmental agencies or reports from third parties.

Under China's current regulatory system, a national security review filing applies only to mergers and acquisitions involving Chinese companies and foreign investors under circumstances provided

under the 2011 Rule. The 2011 Rule prescribes that a foreign investor must apply for a national security review if the investor acquires equity in, and/or assets of, a domestic enterprise in China. In contrast, a transaction between two foreign parties involving interests in Chinese companies is not subject to the national security review requirement.

TYPES OF DEALS REVIEWED

MOFCOM has circulated an unofficial list of industries in which a national security review for a foreign investment transaction is likely to be triggered. These industries mainly include military or military-related products or services, national defense-related products or services, agricultural products, energy, resources, infrastructure, significant transportation services, key technology and heavy equipment manufacturing.

SCOPE OF THE REVIEW

The scope of review focuses on the overall risk profile and impact that various M&A transactions may have on China's national security, defense, economy and public interest.

Foreign investors targeting assets in free trade zones are subject to more stringent national security review rules. The ministerial review panel has wider discretion to terminate or restrict foreign investment transactions in these zones because, while the 2011 Rule gives the panel authority to review foreign investors that obtain "actual control" over companies in the industries listed above, rules governing free trade zones indicate that the panel is allowed also to regulate any foreign investor that has a "significant impact" on investees within the industries listed above.

Greenfield investments and investments in cultural and internet businesses established within these free trade zones through offshore and other contractual arrangements are also subject to national security reviews.

TRENDS IN THE REVIEW PROCESS

The NSL's promulgation indicates that China is attempting to implement a more structured and comprehensive system to keep a closer eye on economic deals that might have security implications. As of now, it is unclear what direction China's national security review will take due to the lack of implementation measures for the NSL. Further, the NSL specifically discusses the need for the state to pay particular



China's Cybersecurity Law became effective on June 1, 2017. It provides additional national security review requirements and standards for companies engaged in or seeking to engage in network and data operations in China.



attention to cybersecurity and network data protection for national security purposes. Article 25 of the NSL provides that China shall “build a network and information security safeguard system, enhance network and information security protection capabilities... achieve safe and controllable network and core information technology, critical infrastructures and information systems...”

Therefore, as part of China’s overall national security initiative, China’s Cybersecurity Law (the CSL) became effective on June 1, 2017. It provides additional national security review requirements and standards for companies engaged in or are seeking to engage in network and data operations in China. As such, companies must be mindful of the cybersecurity and network protection requirements under the

CSL as the law places additional national security scrutiny for network operators in China.

The CSL primarily focuses on data security protection requirements and standards for critical information infrastructure operators, network operators and financial institutions to protect their networks from interference, damage and unauthorized access, along with the prevention of data leaks, thefts and falsification of information.

The Cyberspace Administration of China (CAC) serves as the primary governmental authority supervising and enforcing the CSL. A tiered network security protection will be further introduced in the future and various network operators shall comply with their corresponding level of network security requirements.

The CAC has issued various measures to supplement and

clarify certain requirements of the CSL. Some of them are still in the proposed draft form. In particular, on April 11, 2017, the CAC published a draft proposal, Measures for the Security Assessment of Outbound Transmission of Personal Information and Critical Data, together with the draft guideline on the valuation methods in August 2017. These draft rules extend the data localization requirement under the CSL for critical information infrastructure operators to other network operators, requiring such operators to undergo security assessments in order to transfer data to destinations outside of China. At this point, these drafts have not been published as final regulations; however, they represent a real possibility of what the final regulations could require.

Besides the rules on trans-border data transmission control, the

Measures for the Security Review of Network Products and Services was finalized and came into effect along with the CSL on June 1, 2017, which provides detailed provisions regarding the security review standards of network products or services purchased by critical information infrastructure operators that may affect national security. The measures focus on verifying whether such products or services are “secure and controllable” and the review process will take the form of a security risk assessment of the products or services purchased by these operators. In light of the above, we expect that China will continue to issue implementation and national security review standards and requirements under the CSL, specifically targeting companies seeking to operate as critical information infrastructure operators or other network operators in China. In light of the NSL and the CSL, foreign investors should continue to monitor the developments of China’s national security review process.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

Until issuance of implementation rules to the NSL, foreign investors should continue to be mindful of the terms and conditions of the 2011 Rule and pay special attention to transactions that might fall within the industries that are likelier to trigger national security concerns for MOFCOM. Buyers should also be cautious when completing transactions before obtaining a national security approval, since buyers might be forced to divest the acquired assets if the transaction ultimately fails the security approval process. Due to enforcement uncertainties and the broad scope of captured industries, foreign investors interested in sensitive industries often schedule voluntary meetings with MOFCOM officials to determine the national security review risk before commencing the formal application process.

REVIEW PROCESS TIMELINE

The timeline used in practice and details of the national security review process in China are unclear, as information related to each individual application is not publicly available. The notional timeline below is based on the 2011 Rule:

MOFCOM will submit an application to a ministerial panel for review within five working days if the application falls within the scope of review.

The panel will then solicit written opinions from relevant departments to assess the security impact of the transaction. It could take up to 30 working days to complete the general review process.

The panel will then conduct a special review of the application if any written opinion states that the transaction may have security implications and will conduct a more detailed security assessment of the overall impact of the transaction. A final decision from the review panel will be issued within 60 working days of the start of the special review.

2018 UPDATE HIGHLIGHTS

- The CSL became effective on June 1, 2017. The CSL primarily focuses on the security protection of data and information for critical information infrastructure operators and other network operators.
- Throughout 2017, the CAC issued various draft and final measures aiming to provide more clarity to the CSL and the scope of its implementation. The CAC also made multiple proposals for public comment on additional measures aiming to extend the data localization requirement under the CSL to cover other network operators, which would require all such operators to undergo security assessments in order to transfer data to destinations outside of China.
- We expect to see further developments and clarification on the scope and impact of the CSL in the near future, and companies should keep a close eye on how the measures proposed and finalized by the CAC under the CSL would affect their business and operations going forward.

OUTCOMES

Generally, the outcomes of a national security review are as follows:

- The investment may be approved by MOFCOM, including with mitigation conditions
- MOFCOM will terminate a foreign investment project if it fails the national security review
- If the Chinese government has national security concerns about a transaction that is not submitted for approval, parties could be subject to sanctions or mitigation measures, including a requirement to divest the acquired Chinese assets
- A foreign investor may withdraw its application for national security review only with MOFCOM’s prior consent
- Decisions resulting from a national security review may not be administratively reconsidered or litigated

Japan

Japan's implementation of the 2017 amendments to FEFTA must be watched closely to see whether Japan will adopt a more aggressive stance

By Jun Usami, William Moran and Fumika Cho

Under the Foreign Exchange and Foreign Trade Act (FEFTA), the Ministry of Finance (MOF) and the relevant ministries with jurisdiction over the transaction matter review foreign investments, including acquisitions of Japanese businesses by foreign persons or businesses. The Ministry of Economy, Trade and Industry (METI) also enforces FEFTA.

WHO FILES

FEFTA requires a "Foreign Investor" to submit an advance notice or a post-transaction filing depending on the type of the business in which the target entity is engaged or the nationality of the Foreign Investor, through the Bank of Japan to MOF and relevant ministries. Foreign Investors include:

- Any individual who is a non-resident of Japan
- Any entity established pursuant to foreign laws, or other entities having their principal office in a foreign country
- Any entity in which 50 percent or more of the voting rights are held by an individual or entity described above
- Any entity in which the majority of directors or the representative directors of the entity are individuals who are non-residents of Japan

TYPES OF DEALS REVIEWED

The MOF and the relevant ministries review two types of transactions: Inward Direct Investments and Designated Acquisitions.

An Inward Direct Investment includes, among others, the acquisition by a Foreign Investor of shares of a Japanese unlisted company (including initial incorporation) from resident shareholders, as well as the acquisition by a Foreign Investor of shares of a Japanese listed company, resulting in the Foreign Investor's holding of 10 percent or more of the listed company's shares. An Inward Direct Investment also includes a Foreign Investor's lending to a Japanese company, and a Foreign Investor's purchase of company bonds of a Japanese company if and so long as the amount and term thereof exceeds a certain threshold. There are a few more variations of the transaction that fall into Inward Direct Investments.

A Designated Acquisition is a transaction where a Foreign Investor acquires shares of a non-listed company from other Foreign Investors.

With respect to Inward Direct Investments, almost all transactions (with some statutory exceptions) require post-transaction filings, unless advance notice as described below is required. Transactions requiring advance notice are subject to review and approval by the MOF and the relevant ministries. Investment from certain countries or in certain designated industries (e.g., airplanes, weapons, nuclear power, agriculture, forestry and fisheries, and the oil industry) are designated as transactions that may affect national security, public order or public safety of Japan, or may have a significant adverse effect on the Japanese economy, and consequently require advance notice filings. Regarding Designated Acquisitions, a Foreign Investor is required to submit advance notice if the target company is engaged in the business related to Japan's national security (i.e., the target company falls in a designated industry such as airplanes, weapons and nuclear power). Post-transaction filings are not required for a Designated Acquisition.

SCOPE OF THE REVIEW

For reviews of Inward Direct Investments and Designated Acquisitions that require advance notice, the MOF, METI and the relevant ministries issued a public



In response to the increasing complexity of foreign investment, FEFTA was amended to place new restrictions on Designated Acquisitions, from October 2017 onward, which are equivalent to those placed on Inward Direct Investments.

announcement in August 2017 clarifying the factors to consider. The factors include:

- Whether the production base and technology infrastructure in Japan can be maintained vis-à-vis Japan's security-related industries
- Whether outflow of sensitive technology important for security can be prevented
- Whether public activities during peacetime and emergency can be maintained
- Whether public safety can be maintained
- How the attributes of the financial plan and past investment behaviors of the Foreign Investors and their affiliates look, etc.

TRENDS IN THE REVIEW PROCESS

The ministries have approved almost all of the notified transactions in the past. The only known case where a transaction was blocked was in 2008 when a foreign investment fund planned to acquire 20 percent of the shares of a power company, which had a nuclear power plant. In response to the advance notice made by the fund, the MOF and METI recommended that the acquisition not be allowed, because of the perceived risk that the transaction might disturb the maintenance of the public order in Japan. However, because the fund did not follow the recommendation, the MOF and METI ordered the fund to discontinue the acquisition. The fund did not appeal the order.

Before October 1, 2017, only Inward Direct Investment transactions were reviewed.

However, in response to the increasing complexity of foreign investment, FEFTA was amended to place new restrictions on Designated Acquisitions, from October 2017 onward, which are equivalent to those placed on Inward Direct Investments. In addition, the amended FEFTA has also introduced enforcement measures for the breach of those restrictions. For

example, if a Foreign Investor does not give advance notice as required by FEFTA or does not obey the recommendation or orders issued by the MOF and the relevant ministries, the ministries are authorized to order the disposal of shares obtained in the transaction.

HOW FOREIGN INVESTORS CAN PROTECT THEMSELVES

Although there is no specific provision regarding the procedures for mitigation measures in FEFTA and related laws or orders, the MOF and the relevant ministries are allowed to require mitigation measures, which are assumed to be negotiated with the Foreign Investor. That said, Foreign Investors can proactively propose and negotiate mitigation measures with the ministries in charge.

REVIEW PROCESS TIMELINE

A Foreign Investor who has made an advance notice filing cannot close the transaction until the expiration of 30 calendar days from the date the MOF and the ministry having jurisdiction over the transaction received the notification. However,

for certain transactions, such as greenfield transactions and roll-over transactions, the waiting period is usually shortened to two weeks. The MOF and the relevant ministries can extend the waiting period up to five months, if it is necessary for the review.

If the MOF and the ministry with jurisdiction find the reviewed transaction problematic in terms of national security, they can recommend that the Foreign Investor change the content of the transaction or discontinue the transaction after hearing opinions of the Council on Customs, Tariff, Foreign Exchange and other Transactions. The Foreign Investor after receiving such recommendation must notify the MOF and the ministry with jurisdiction of whether it will accept the recommendation within ten days.

If the Foreign Investor does not provide notice or refuses to accept the recommendation, the MOF and the relevant ministries may order the modification of the content of the transaction or its discontinuance before the expiration date of the waiting period.

OUTCOMES

- Almost all deals are approved
- The October 2017 FEFTA Amendment introduced new restrictions to transfer of shares in non-listed companies from a Foreign Investor to another Foreign Investor (i.e., out-out transfer)
- The October 2017 FEFTA Amendment also introduced an enforcement mechanism addressing the breach of the restriction thereunder, which was not available before the amendment
- Although almost all deals continue to be approved and there is no apparent change to enforcement practice, Japan might join the global trend of aggressive enforcement

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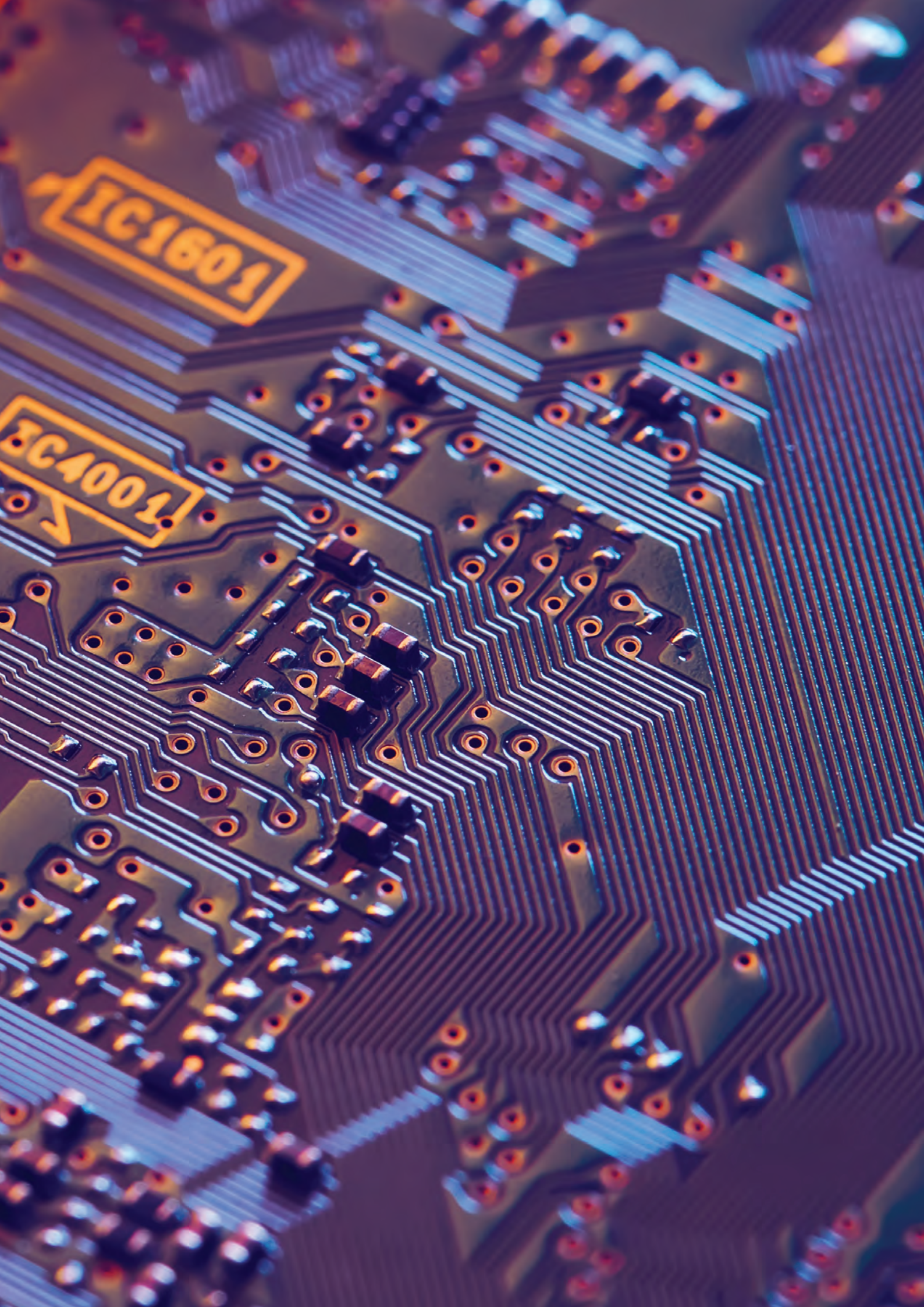
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