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AD TALKS ON FOREIGN DIRECT INVESTMENTS CONTROL IN FRANCE

Real Estate and Construction Environmental Law Public Law and Public Procurement Law Private Equity M&A | 22/06/20 | Julien Aucomte Vincent Brenot

On Wednesday 17 June 2020, in the context of an AD Talks, August Debouzy law firm was pleased to welcome Mr Antonin Nguyen, Head of the Foreign Direct Investment Office ("**FDI Office**") of the French Ministry of the Economy and Finance (also known as Multicom 4) since 2018.

This conference was an opportunity for Mr. Nguyen to present the main principles of foreign direct investment control in France (1.), with a focus on recent legislative and regulatory developments in this field (2.), and on the impact of the COVID-19 crisis (3.).

1. The main principles of foreign direct investments control in france

Mr. Nguyen started his speech by underlining that foreign direct investments ("**FDI**") in France are, and will remain, in principle, free. The free movement of capital is enshrined in Article 63 of the Treaty on the Functioning of the European Union ("**TFEU**") and Article L. 151-1 of the French Monetary and Financial Code ("**FMFC**"). This principle involves that the FDI control mechanism must remain an exception. Thus, FDI control can only be carried out to address certain issues that justify such a restriction on the free movement of capital (protection of the public order and safety and interests of national defence).

Mr. Nguyen emphasized that the purpose of such control was not to hinder the implementation of FDI but, on the contrary, to facilitate their implementation and sustainability by allowing an upstream dialogue between the national authorities and the investor. In the context of this dialogue, the administration identifies the activities that are critical for the State and let them know to the investor.

in order to identify the sensitive activities of the target entity that are critical for the French State.

France has chosen to use the following three cumulative criteria to determine whether an investment falls within the scope of FDI control:

- the nationality of the investor (individual or legal person). If the investor is of foreign nationality, the first criterion is of course met;

- the nature of the contemplated investment:
  - the takeover, within the meaning of Article L. 233-3 of the French Commercial Code, of an entity under French law;
  - the acquisition of all or part of a business ("*branche d'activité*") of an entity governed by French law;
  - the crossing, directly or indirectly, alone or jointly, of the threshold of 25% of the voting rights of an entity governed by French law (this condition is not applicable for EU Member State investors);

- the sensitivity of the business activity of the targeted entity by the FDI. This means that if the target entity's activity is listed in Article R. 151-3 of the FMFC (see below), an authorisation (simple or conditioned) will be required if the other two criteria are also met.

The two first criteria relating to the nationality of the investor and the nature of the operation are analysed by the FDI Office, which employs five agents in addition to Mr. Nguyen.

Mr. Nguyen also specified the methods for assessing the second criterion relating to the nature of the contemplated investment, particularly in case of a chain of entities which includes foreign shareholders. The FDI Office retains a strict interpretation of Article L. 233-3 of the French Commercial Code: thus, any linked entity in the chain of control is considered as likely to acquire the control over the target entity, which means that the administration is not only interested by the nationality of the sole "*parent*" entity but of any entity in the chain of control of the target company. In other words, even if a French entity controls the entire chain as final shareholder, as soon as there is a foreign entity in the chain of control, the foreign nationality criterion will be considered as met.

Once this analysis is carried out, the FDI Office consults with the state departments involved in the sector of activity concerned by the operation which are part of the Interdepartmental Committee of Foreign Investments in France ("*Comité interministériel des investissements étrangers en France"),* such as, for instance, the Directorate General of Armament when the entity operates in the defence sector, to determine the degree of "*criticality*" of the target's activity. The FDI Office may also seek the opinion of the major operators in the sector at stake, under strict confidentiality. The analysis of the sensitivity of the activity involves determining the consequences on the entity's activity sector, using a range of clues to determine the long-term impacts of the operation.

In response to an attendee's question, Mr. Nguyen replied that there is currently no publicly available doctrine that would explains how the criteria are apprehended by his services. However, he did not rule out the possibility that such doctrine might eventually be published, in the form of a circular or guidelines. However, regarding the preparation of a compendium of the FDI Office's decisions, he indicated that this was not an option due to confidentiality reasons. However, Mr. Nguyen noted that the recent reform of the control of FDI clarified the typology of conditions that could be attached to an investment authorisation.

Mr. Nguyen also stressed out that the decisions of the Minister of the Economy and Finance could be appealed before the administrative judge. However, very few appeals have been brought before court because of the sensitive and casuistic nature of the administrative decision in question. From a procedural standpoint, Vincent Brenot highlighted that the investor would have to demonstrate that the administration committed a manifest error of assessment, that the administrative judge, who is not be entitled to substitute the administration, is often reluctant to sanction. Mr. Nguyen thus indicates that the administration has won the rare cases brought against the administration's decisions.

Finally, concerning the international cooperation on FDI control, the FDI Office works with other States in confidential meetings and carries out benchmarks on foreign regulations.

At the European Union level, the Regulation 2019/452 of 19 March 2019 *establishing a framework for the screening of FDI into the EU*, which will take effect on 11 October 2020, will enable the implementation of greater cooperation and effective coordination between Member States. The regulation contains various provisions designed to strengthen the cooperation between Member States and the European Commission, such as the implementation of an alert mechanism between Member States and the possibility of requesting opinions from the Commission and local authorities in charge of controlling FDIs.

2. The recent reforms implemented since 018

The tightening of the FDI control legislation at the international level has led France to strengthen its legal framework in this area. The reforms also include certain easings and procedural improvements.

This motion was initiated with the adoption of Decree n° 2018-1057 of 29 November 2018 *on foreign investment subject to prior authorisation*, which extends the scope of authorisation to certain sensitive technologies.

Though, the most important reform was the adoption of Act n° 2019-486 of 22 May 2019 *relating to the growth and transformation of societies* (known as the "***Pacte Act***"), which has brought a deep change of the legislative framework on several points:

- the coercive powers of the Minister of the Economy and Finance are increased. The Minister now has greater coercive powers and a wide range of actions for precautionary measures in the event of an investor's failure to comply with FDI regulations;

- the Minister of the Economy and Finance may also regularise transactions carried out without prior authorisation, enabling to lift the nullity of the project;

- the administration can be provided by the investor with any useful document necessary for the exercise of its mission. No secrecy can be invoked, in particular the professional secrecy;

- the transparency of the procedure is improved with the establishment of a clear framework for discussion between the Parliament and the Government in strict compliance with confidentiality obligations.

Decree n° 2019-1590 and Ministerial Order of 31 December 2019, which came into force on April 1st, 2020, reformed the entire regulatory framework. The purpose of those regulations is to simplify and unify the FDI control screening procedure, in particular regarding the sensitive activities subject to control and the definition of an investor.

In more concrete terms, the above-mentioned regulations seek to strengthen the control of the Minister of the Economy and Finance. This tightening of regulations takes several forms:

- an enlargement of the scope of sensitive activities subject to authorisation was decided to include food safety, the written and digital press for political and general information and certain critical technologies;

- the lowering of the control threshold from 33% down to 25% of the voting rights of the target entity, which resulted in a higher number of operations being included in the scope of the authorization. Furthermore, for an investor to be deemed European and exempted from the application of this threshold, it must hold a European nationality and not be controlled by a non-European holding entity. It makes it now possible to control the indirect crossing of the threshold, through an European subsidiary;

- a clarification of the responsibilities with the obligation to designate, within a chain of control, the investor who will assume the responsibilities attached to this quality. This provision makes it possible to better involve investors and make them responsible;

- the communication by the investor of its links with foreign States in order to better consider sovereign investment strategies for the issuance of the authorisation. The investors must disclose whether their capital is

controlled or owned by a sovereign State, as well as any public subsidies received, or public procurement contracts obtained.

The regulatory texts have also provided procedural clarifications:

- the conditions attached to authorisations may be amended or even abolished if the investor demonstrates that they are no longer necessary, for example, in the event of technological developments that rendered the sensitive nature of the activity obsolete. The request for amendment of the conditions attached to the authorisations can also be initiated by the Minister in charge of the Economy;

- the conditions of the authorisations are set in accordance with the broad objectives of the regulations. Mr. Nguyen pointed out that these conditions were very often the preservation of the activity in France, the obligation to appoint French managers in the event of possession of confidential information or the establishment of the head office in France. However, French law excludes the possibility for shareholders to be deprived of their rights, which excludes the implementation of American like "*proxy boards*" designed to isolate the sensitive activity entity from its shareholders. The leverage of action regarding shareholding would consist in setting up a security committee that could be interposed in the governance of the company, to review strategic decisions and even oppose to some of them;

- the procedure is now divided into two phases: a first phase of thirty days to examine the criteria for determining whether the transaction falls within the scope of the screening procedure, and if so, whether it is necessary to attach conditions to the authorisation. At the end of this first phase, for complex operations requiring conditions, a second forty-five-day phase begins, which leads to an authorisation or a refusal. Processing times can be very fast for the least complex cases (about three weeks) but can be of several months in the case of large operations. Mr. Nguyen stressed out that compliance with deadlines depends on the diligence of the administration, but also of the investor, and that the FDI Office systematically tries to respect the transaction's timetable and to issue the authorization before the closing the investor contemplated, provided it is compatible with the analysis timing;

- another procedural novelty introduced by the decree was to allow target companies to request an opinion from the administration on the planned operation. This request relates only to whether the activity is sensitive or not. It allows the administration to have an upstream overview of the planned operations and thus offers a most welcome flexibility to the State and a better visibility for the companies at stake in view of a transaction on their share capital;

- finally, the regulations introduce the possibilities for exemption from authorisation for intra-group transactions, when the investor reaches the 25% threshold after having acquired control following an authorisation issued under the FDI control regulation, or conversely, when he acquires control following an authorisation and then crosses the 25% threshold.

Mr. Nguyen recalled that while the conditions were sometimes referred to as "*commitment*", they were nonetheless real obligations that the investor must respect in order to retain the benefit of its authorisation.

Asked by one of the participants about the links between merger control and FDI control, Mr. Nguyen recalled that the two procedures have different purposes. However, the FDI Office considers competition law issues when analysing the "*criticality"* of the transaction to assess the substitutability of a product or service or the assessment of the risks for the French interests, particularly with regard to internal competition issues, such as when an investor owns an industrial site abroad similar (i.e. potential competitor) to the one he seeks to acquire in France.

3. The impact of the sanitary crisis

The health crisis caused by the Covid-19 epidemic weakened the national economy and led France to set up temporary complementary mechanisms.

In a communication dated 25 March, the European Commission urged States to be vigilant and to strengthen their legal framework for the control of FDI. There has been an overall strengthening of FDI control in all countries.

The April 27, 2020 decree *on foreign investment in France* includes biotechnology in the scope of FDI control.

The Minister of the Economy and Finance also indicated that the threshold for the acquisition of shareholdings was to be lowered to 10% of the voting rights in a listed entity operating in a sensitive sector. This temporary measure, which should remain in force until December 31, 2020, will also lighten the review procedure since that, following a very light application, the Minister of the Economy and Finance will only have ten days to decide whether or not the transaction requires a prior authorisation so as not to penalise French companies that need a fast capital in-flows. Unless otherwise stated by the administration, the investor will be excused from filing a proper authorization request. The draft decree embodying this system was recently examined by the *Conseil d'Etat* (the French administrative supreme court which also acts as counsellor to the Government) and will be published before the end of the month.

In connection with the health crisis, Mr. Nguyen also answered to a question about the public health protection sector. He specified that this sector is considered sensitive since Decree n° 2014-479 of May 14, 2014 *on foreign investment subject to prior authorization* and aims to protect certain drugs or vaccines based, for instance, on a classification

established by the World Health Organization and by the National Agency for Drug Safety.

Conclusion

Mr. Nguyen indicated that the FDI Office had examined more than 200 files in 2019, knowing that 1 468 projects have been identified by *Business France*: thus, between 14 and 15% of FDI have been controlled. Most of the operations were authorised (with or without conditions).

In very rare cases, the project was profoundly reconfigured, i.e. the investor had to give up the acquisition of certain sensitive activities. In an even lower number of cases, authorisation was not given by the Minister of Economy and Finance either because, after discussions with the State, the investor preferred to abandon the project because of its disagreement with the conditions imposed by the administration, or because the State simply was not in favour of the project.