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UK Is Left out of EU Cooperation on Foreign Direct Investment, And Will Soon Be "Foreign"

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Foreign Direct Investment Regulation

The EU Regulation on Foreign Direct Investment (2019/452) (the "**EU FDI Regulation**") will enter into force fully on October 11, 2020. Most notably, on this date, a cooperation and information sharing mechanism among Member States and the European Commission in respect of foreign direct investment ("**FDI**") that has an "EU-dimension" will come into effect.

As October 11 approaches, there is renewed attention on how the EU cooperation and information sharing mechanism will operate in practice and impact upon transactions entered into by foreign investors in the EU.

In addition, many EU Member States have been making preparations to ensure that their domestic laws permit the gathering and sharing of information on FDI to a degree necessary to engage in such cooperation activities among EU partners and the European Commission. In Sweden, for example, a recent legislative proposal has provided for implementation of the EU FDI Regulation in the near-term, while wider ranging measures that will otherwise enhance and update FDI laws and screening powers in Sweden are proposed to be brought into law at a later date.

In this Alert, we consider the implementation of the EU FDI Regulation in the UK particularly, and in light of the forthcoming end to the Brexit transition period.

UK Not a Member State for EU Cooperation on FDI

It has recently become clear that the UK will not participate in EU-level cooperation and information sharing in relation to FDI. This will be the case even prior to the end of the transition period for Brexit. Specifically, on July 31, 2020, the European Commission adopted a formal decision that the UK is not to be treated as an EU Member State for those aspects of the EU FDI Regulation that concern the cooperation and information sharing mechanism for FDI that has an EU-dimension.

In making the decision, the European Commission relied upon a provision of the Withdrawal Agreement for the UK's departure from the EU, which permits derogations from the general and overarching principle that all references in EU law to "Member States" are to be understood to include the UK during the transition period. That derogation can only be applied in circumstances where there is an information exchange or procedure that would continue to be implemented after transition, and that would give the UK access to security-related sensitive

information that is considered suitable only to be made available to (other) Member States, (continuing) EU nationals, and natural or legal persons residing or established in (other) Member States.

The derogation may only be applied on an exceptional basis. In addition, and in accordance with the Withdrawal Agreement, the UK is to be notified of any decision to apply the derogation.

FDI in the UK Post-Brexit

At the same time, the UK had been taking some preparatory steps to cooperate within the EU on FDI. In particular, the UK adopted a short piece of legislation in June 2020 to increase local powers to gather information on FDI for the purpose of cooperating within the EU on FDI, and recently a consultation was opened (and then suspended) in respect of guidance on the exercise of these new powers. Pending clarification from the UK authorities, it now appears that such measures will not be needed in practice.

With the end of the Brexit transition period expected on December 31, 2020, the UK was only expected to be subject to the EU FDI Regulation and the cooperation mechanism for a short period. To cooperate after Brexit on FDI would require at least some voluntary understanding between the UK, the EU institutions and Member States on information sharing, including in respect of highly sensitive matters. What the Commission's recent decision may reveal is a lack of interest in taking any such voluntary step—at least for now.

Overall, the long term picture for regulation of FDI in the UK is one based on a standalone regime to which the EU FDI Regulation has no application. Since June this year, the UK Government has shown increasing focus on its future plans to reform the regulation of FDI into the UK. In prior blogposts, we have discussed, in particular: (i) the prospects for a forthcoming National Security and Investment Bill that is expected to substantially update and amend UK powers to scrutinise FDI and (ii) additional powers to intervene in transactions occurring in the UK adopted quickly this summer in connection with the COVID-19 crisis and future public health emergencies, and in relation to critical technology.

UK As a Foreign Investor Into the EU

The UK will also shortly become a "foreign" country for EU FDI purposes, and UK investors into the EU will have new status as "foreign investors" under many of the FDI laws implemented by the Member States. Faced with this, UK investors may need to sharpen both strategy and due diligence on FDI.

Around half of EU Member States have adopted FDI laws to date, and the Member States that have typically defined "foreign" investors as either non-EU or non-EEA investors—these categories will include UK investors from the end of the Brexit transition period. Only Poland has taken a substantially different approach and exempted all OECD investors from filing obligations under its newly adopted FDI laws.

UK investors (like other foreign investors) will soon need to understand and become accustomed to dealing with these differences in EU Member State FDI laws. The EU FDI Regulation does not harmonise FDI laws in Europe or create a one-stop shop for FDI filings. Rather, the EU FDI Regulation creates a framework of minimum standards for Member State FDI laws and, as an exception, provides for some EU-level cooperation on FDI that has an EU-dimension. As such, filings and scrutiny of FDI occur in the EU primarily at the Member State

level in accordance with local laws, which may differ in scope of application and review procedure.

Once the Brexit transition period ends, there are numerous transaction proposals and structures that UK investors into the EU may need to look at with fresh eyes. FDI filing obligations may arise in relation to both direct and indirect investments into EU Member States. Many of the national FDI regimes in EU Member States have introduced mandatory **pre-closing filing requirements**, similar to merger control and secured by significant **standstill periods**. Failure to file or to close without clearance may be sanctioned with fines, and the absence of a clearance decision can lead to an acquisition being deemed void. Some Member States even have introduced associated criminal sanctions for breach of FDI laws. In addition, in some countries, such as Germany, FDI filings may be required for **intra-group transactions**, including reorganisations—a point to be noted for any multi-national group with UK and EU subsidiaries.

Those best advised will not delay in addressing the changing status of the UK in relation to EU M&A and will look carefully at those transactions being planned in the EU today and that may be executed soon after the Brexit transition period ends.

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