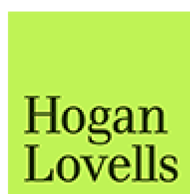

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FD I didn't know that…

Part 1 – Considerations on transaction structures in UK, EU, US and Australia and how to avoid missing filings

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Foreign direct investment (FDI) will continue to be a top order consideration for deal makers and investors for the foreseeable future. As a topic with inherent geopolitical interplay, and each country having a nuanced approach to what is meant by national security and public order, this creates complexity for deal feasibility and execution.

As part of the day-to-day work of the Hogan Lovells Global FDI Practice, clients often express surprise at certain aspects of how FDI regimes function in practice. Either because they are counter-intuitive, or because some regimes function differently from those which are more familiar to them. Complications can then arise due to the fluid nature of the concerns trying to be tackled and the evolving interpretation of more nascent regimes.

The risks of getting an FDI filing assessment wrong can be severe – they can include financial penalties, void transactions and possible criminal liability.

Hogan Lovells' team of experts explore over two articles some of these key areas of which investors, and those active in M&A, need to be aware. In this first article, we consider topics relevant to the initial considerations when assessing the need to make FDI filings. In our second article, we will explore more substantive items and considerations around preparing for closing.

FDI regimes do not necessarily only apply to 'foreign' investors

While the "F" in FDI stands for "foreign", this is conceptually misleading for some regimes. For instance, in the **UK** domestic, i.e. UK-based, investors and acquirers are caught by the need to make mandatory filings on the same basis as those located abroad. Indeed, there have even been some conditional clearance decisions imposed on UK-based investors. Similarly, the **Netherlands** also makes no distinction between Dutch and foreign investors.

Within the **EU**, some regimes – such as **France** – screen and track EU-based investors, while others are exempted from the need to notify in certain circumstances. In **Spain**, the general FDI regime has been temporarily extended, covering certain investments from EU or European Free Trade Association (EFTA) based investors in strategic sectors. Similarly, investment under the sector-specific defence regime are

subject to control both when the investor is not resident in Spain (including EU residents outside Spain) and when it is a foreign natural person resident in Spain.

It is also worth remembering that in addition to individual Member State screening regimes, it is also important to consider the **EU** co-operation mechanism which operates in parallel with which Member States must comply, requiring the exchange of information between Member States and the European Commission.

It is important to keep in mind that most global FDI regimes do not only look at the origin of the direct acquirer, but the whole shareholder chain up to the ultimate beneficial owner (UBO) of the acquiring entity. In the **US**, in some scenarios, the acquisition of a US business by another US business could fall within the jurisdiction of the Committee on Foreign Investment in the United States (CFIUS). For example, an acquisition by a US-organized company of a US business might nevertheless be subject to CFIUS's jurisdiction if the acquiring company is directly or indirectly controlled by one or more foreign persons. Separately, if a US publicly traded company uses a wholly-owned foreign-organized subsidiary to effect the acquisition of a US business, the transaction might be subject to CFIUS's jurisdiction, notwithstanding that the foreign-organized subsidiary is itself controlled by its US publicly traded parent.

An acquisition by a domestic direct acquirer also may qualify even with only limited foreign ownership. For example, in **Germany** an indirect shareholding as low as 10% on any shareholding level (i.e. non-diluted with potentially even less effective shareholding down the chain in the direct acquirer) may trigger FDI filings. In **Spain**, an indirect shareholding slightly above 25%, or the possibility to otherwise exercise direct/indirect control, would require a filing.

Even ostensibly innocuous internal re-organisations may need to be notified

In circumstances where there is no change in the ultimate beneficial owner, and perhaps something as straightforward as a new wholly-owned holding company is being inserted into a structure, a notification may still be required.

This is the case in places such as **Australia, Austria, Belgium, Italy, Sweden, US** and **UK** to name but a few. Whether a specific re-organisation requires notification is fact specific and needs to be carefully considered. Such a scenario can arise also in the context of M&A transactions, e.g. if certain assets or entities are carved-out and grouped together prior to a sale to a third party. In such cases, separate filings for the carve-out and the following acquisition might be required, although from a practical standpoint it may be possible to submit them under one cover letter and ask the authority to review them simultaneously. Conversely, some jurisdictions expressly exclude the need to file internal restructurings, such as **Spain**.

While internal re-organisations are unlikely to raise any substantive concerns, any assumptions that such transactions are exempt from the need to notify would be wrong.

Mind the gap: various forms of investments can be caught – so a 10% acquisition or even miniscule incremental stock-building needs to be considered

In some jurisdictions, the acquisition of as low as 10% of shares can lead to a mandatory filing be required – many Member States in the **EU** capture such low levels of investment. In fact, the more

sensitive the business activities are, the more likely it is that very low shareholding thresholds apply.

Examples for a 10% threshold include **Austria, Belgium, Finland, France** (for listed entities), **Germany, Spain** or **Sweden**. **Italy** has an even lower threshold of 5%. It is worth noting **Spain** has sector-specific regimes, including national defence, where foreign investments of more than 5% of the share capital, or that allow the investor to form part of the management of the company, would be subject to clearance. In the US, CFIUS's jurisdiction does not hinge on any ownership interest threshold, so foreign investments under 5%, for example, could be subject to CFIUS's review, depending on the investor rights acquired and the type of US business. This brings classic investment rounds in companies with covered activities into the scope of potential filing requirements.

Shareholder rights can also have an impact on the filing percentage thresholds; for example, in **Australia** certain shareholder veto rights or director appointment rights can in themselves trigger a filing obligation or lower the filing threshold to even a nominal percentage interest.

Another important factor to keep in mind is that, at times, even miniscule, incremental investments may trigger a filing obligation if they are done in the context of stock-building. For instance, **Germany** has several thresholds potentially triggering FDI filings once an investor reaches 10%, 20%, 25%, 40%, 50% or 75% of the total voting rights in the target company, even if a total of less than 10% is acquired in an individual transaction. Other countries, such as the **UK** and **Italy** also capture stock-building.

In addition, in **France**, the acquisition of a part of a business (such as a business unit), as well as the acquisition of a French branch, may trigger a French FDI filing if other conditions are met.

In or out? The need to have a physical presence in a country can be flexible

Some jurisdictions have very broad jurisdictional scope, catching transactions which may have relatively limited nexus to that country. At its most extreme, sales into a country, or a non-domestic entity contracting with government, can be sufficient to trigger a filing. This is the case in places such as the **UK, Czechia** and **Italy**. For any multi-jurisdictional filing analysis it is therefore important to not only review the full organisational chart to identify all entities and branches, but also expressly to request information about sales into certain jurisdictions, such as those above, in order to thoroughly analyse filing requirements.

Transactions which do not have a clear impact in a certain jurisdiction, and which might be considered 'foreign-to-foreign' transactions, may still need to be notified. For instance, in **Belgium**, sales to **Belgian** customers are not required. That could result in a filing requirement for a Belgian software company which employs software engineers that only work on internal global projects, provided that the employees' activities are caught, e.g. in the AI space, which is also true for the **UK**. Such circumstances include domestic transactions in which the target has a subsidiary in another country – namely, a foreign person's indirect investment in, or acquisition, of a subsidiary. This is the case for many jurisdictions including the US.

Tell me who you are and I will tell you if you need to file

In **Australia**, the identity of the investor/acquirer can be determinative and can even catch an overseas transaction if the investor is a 'foreign government investor' . This concept is very broad with private

equity/infrastructure funds potentially being classified as 'foreign government investors' if their limited partners include a significant proportion of government related investors, such as sovereign wealth finds or state pension funds. In part this accounts for the comparatively high number of FDI filings made in Australia compared with other jurisdictions.

Similarly, in **Spain** if an investor meets certain subjective characteristics, such as being controlled by a foreign government, a filing may be required irrespective of the sector in which the target is active. It is also necessary to assess on a case-by-case basis where the investor has made investments in companies in another EFTA or Member State where they are active in sectors affecting security, public order and public health (especially in strategic sectors).

In the **UK**, there are also some very limited circumstances in which a mandatory filing may turn on whether the investor/acquirer itself generates or aggregates electricity.

Conversely, there are some jurisdictions which exempt acquirers with a certain background from filings. In **Poland**, investors from Organisation for Economic Co-operation and Development (OECD) member states do not have to notify. Also, the new **Bulgarian** FDI screening regime contains some far-reaching exemptions for "low risk" investor countries, which include NATO allies such as the US, the UK, or Canada, but also Australia, New Zealand, Japan, South Korea, the UAE, and Saudi Arabia.

Certain PE structures and acquisitions can be caught

There is apparent divergence between regimes on how to deal with and assess PE structures and assessments, which creates complexity for multi-jurisdictional deals.

Many regimes capture transaction structures and transactions which intuitively one might assume would not be. For example, a continuation fund – managed by the same private equity management entity and with similar (or even the same) passive limited partner investors in the new fund – may still need to be notified on a mandatory basis. This is currently the case in places like **France** and **UK**.

There is no one size fits all when it comes to FDI and the categories above are just examples of how parties to transactions might be surprised about the ways in which their transactions interact FDI regimes. The Hogan Lovells Global FDI Practice has a team of experts which help clients navigate through these complexities on a daily basis as a partner vital for change. Our unrivalled in-depth insight and global reach allow us to navigate potential issues before they arise and advise on ways to mitigate the impact on deal timetables. We operate at the intersection of business and government on FDI issues and indeed advise both.

Please do get in touch if you would like to discuss how we can help you.

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