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M&A During the COVID-19 Crisis — European Commission Encourages Protection of Critical Assets by EU Member States

The European Commission Issues Guidelines Calling for Heightened Scrutiny of Foreign Investments in the EU

SUMMARY

On 25 March 2020—10 days after the news broke about an alleged US attempt to acquire a German biotech company developing a vaccine against the coronavirus[1]—the European Commission issued a guidance paper to the 27 EU Member States regarding investments by non-EU (*foreign*) entities in strategic industries (the **Guidelines**).[2]

The previous actions taken by the European Commission in the wake of the COVID-19 crisis focused on adapting the bloc's *internal* rules governing state aid. The Guidelines, however, address the EU's *external* relations, encouraging Member States to prevent a sell-off of Europe's strategic assets, including protecting certain companies having capital market valuations well below their "true value".

The Guidelines are not legally binding but will effectively result in increased national scrutiny of foreign investments (including the acquisition of minority stakes)—using existing foreign investment screening mechanisms or any other tools Member States may have to ensure the "continued critical capacity of EU industry" in and beyond the healthcare sector.

A foreign investment review by a Member State may impact the deal timeline and its outcome could vary from an outright prohibition to mitigating measures (such as supply obligations) being imposed by the reviewing national agencies. Consequently, parties to global transactions negotiating risk allocation and

deal value now, more than ever, must plan ahead, mapping out as early as possible the political and strategic sensitivities across a number of jurisdictions.

BACKGROUND AND SCOPE OF THE GUIDELINES

In the EU, the Member States have the power to intervene against foreign investments only where such investments create a risk to security or public order across the EU or in an individual Member State. To date, 14 Member States have foreign investment screening mechanisms in place.[3]

The European Commission's powers, introduced in 2019 and taking effect as of 11 October 2020, are currently limited to issuing non-binding opinions, monitoring and coordinating information exchange across the various national regimes.[4]

The Guidelines do not introduce any new powers for the Member States or for the Commission, but they are likely to have an instant practical impact. In fact, remarkably, they precede the coordinating role that the Commission is scheduled to acquire as of 11 October 2020.

Moreover, and critically, the Guidelines convey the message that immediate action is required to ensure that foreign investments do not risk harming the EU and its capacity to cover the needs of EU citizens. In more detail, the Guidelines:

- Recall that under EU case law, intervention against free movement of capital can be justified on the basis of overriding reasons of general interest such as public health, protection of consumers and preserving the financial equilibrium of the social security system.
- Urge the 13 Member States without screening mechanisms to "*set up a full-fledged screening mechanism and **in the meantime to use other available options** to address cases where the acquisition or control of a particular business, infrastructure or technology would create a risk to security or public order in the EU, including a risk to critical health infrastructures and supply of critical inputs*."
- Call on the 14 Member States with existing screening mechanisms to make full use of their powers and "*take fully into account the risks to critical health infrastructures, supply of critical inputs, and other critical sectors*."
- Emphasize that foreign investment in companies of general interest to the EU, or in companies having received EU funding, should be subject to closer scrutiny.
- Remind investors and targets that foreign investments can be subject to retroactive review and regulatory measures for up to 15 months after consummation (e.g., a transaction closing in March 2020 could be subject to action until June 2021).
- Encourage Member States to apply screening measures also to the acquisition of minority stakes/portfolio investments, and to adopt measures preventing acquisitions by foreign investors that focus on distressed companies.[5]

COMMENTARY

While the Guidelines stress that the EU wishes to remain an open market and attractive to foreign investments, they memorialize the accelerated policy shift in the EU (and other open economies) towards increased scrutiny of foreign investments in relation to strategic assets, including through minority shareholdings.

Consequently, although a large part of future foreign investments in the EU are likely to remain unaffected, the Guidelines are a fresh reminder that careful planning and early constructive engagement with national regulators will be critical for deal certainty and successful value realization in transactions involving sensitive underlying assets.

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ENDNOTES

1 See e.g., https://www.theguardian.com/world/2020/mar/16/not-for-sale-anger-in-germany-at-report-trump-seeking-exclusive-coronavirus-vaccine-deal

2 Guidance to the Member States concerning foreign direct investment and free movement of capital from third countries, and the protection of Europe's strategic assets, ahead of the application of Regulation (EU) 2019/452 (FDI Screening Regulation) 2020/C 99 I/01 (25 .

3 A full list of national screening mechanisms and links to national legislation is kept by the Commission at https://trade.ec.europa.eu/doclib/docs/2019/june/tradoc_157946.pdf

4 See the S&C publication of 15 April 2019 – New EU Regulation Focuses on Cooperation Between Member States and the EU Commission

5 In addition, the Guidelines remind Member States that they can, in certain cases such as a pandemic, intervene by for example imposing compulsory licenses on patented medicines.

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CONTACTS

Brussels		
Michael Rosenthal	+ 32 2896 8001	rosenthalm@sullcrom.com
Foad Hoseinian	+ 32 2896 8028	hoseinianf@sullcrom.com
London		
Juan Rodriguez	+ 44 207 959 8499	rodriguezja@sullcrom.com
Axel Beckmerhagen	+ 44 207 959 8418	beckmerhagena@sullcrom.com