

France Completes Major Foreign Investment Reform

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On December 31, 2019, the French government issued decree n° 2019-1590 (the 2019 Decree), together with an administrative order of the same date (the Order), that comprehensively reshaped French foreign investment rules (as amended, the New Rules) and introduced significant reforms to the French foreign investment review process. The 2019 Decree and the Order are the last steps of a reform that was launched by the French government in 2018 to strengthen French foreign investment control.¹

Specifically, the 2019 Decree: (1) expands the scope of French foreign investment control by redefining certain key operative terms and concepts; (2) enhances the French foreign investment process by establishing a new ruling mechanism, a two-step review process and advance filings and by allowing international cooperation; and (3) clarifies the conditions under which the French Minister of Economy (the Minister) may approve or reject an authorization request and apply sanctions and remedies against defaulting foreign investors.

Similar to efforts in other countries, most notably in the United States with the U.S. Congress' enactment of the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA), the 2019 Decree represents a significant expansion, and formalization, of the foreign investment rules in France.

The 2019 Decree comes into force on April 1, 2020.

Expansion and Clarification of the Scope

Single Definition of Foreign Investor

The French foreign investment regime historically has applied different rules for foreign investors based on whether the relevant investor was domiciled in or outside the European Union or the European Economic Area (EEA). The 2019 Decree has, in large part, abolished the distinction between European and non-European investors. The 2019 Decree defines a foreign investor (Foreign Investor) as follows:

1. any individual of foreign nationality;
2. any individual of French nationality who is not tax-domiciled in France;
3. any foreign-registered entity; or
4. any French entity that is under the control of one or more persons or entities listed above.

Introduction of a Concept of Chain of Control

Under the New Rules, a “chain of control” includes an investor referred to in item (3) or (4) above and any persons or entities that exercise control over such investor. The 2019 Decree specifies that any person or entity that is part of the chain of control will be considered to be a Foreign Investor for purposes of French foreign investment rules.

As a matter of practice, the presence of any Foreign Investor in a chain of control that also includes French investors will trigger French foreign investment control even if the relevant Foreign Investor is ultimately controlled by a French person or entity. This is an important point that French private equity investors using a foreign holding structure for the purpose of a particular transaction should bear in mind. The French authorities

¹ Please see our client alert “[Foreign Investment Control Reforms in Europe](#)” for the initial reforms implemented under decree n° 2018-1057 of 29 November 2018 (the 2018 Decree) and the Action Plan for Business Growth and Transformation Act of May 23, 2019 (the PACTE Law) (Section on France).

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have signaled that in this case, they will have a keen interest in knowing which entity or entities in the chain of control participated in the decision-making process related to the proposed foreign investment.

Extension of the Concept of Control to ‘Significant Influence’

Prior to the 2019 Decree (the Old Rules), “control” was assessed pursuant to article L. 233-3 of the French Commercial Code (FCC). Under these provisions, “control” means (1) direct or indirect holding of a majority of voting rights, (2) *de facto* control (*i.e.*, the ability of a shareholder to effectively determine decisions taken at shareholders’ meetings through voting rights held by such shareholder), and (3) the power to appoint or remove a majority of management or supervisory board members.

The 2019 Decree expands the concept of control to “significant influence.” Under the New Rules, if the French authorities are unable to assess control on the basis of article L. 233-3 of the FCC, they may refer to the provisions of paragraph III of article L-430-1 of the FCC. This article states that

control arises from rights, contracts or any other means that confer, either alone or in combination with others, and taking into account the relevant factual or legal circumstances, the possibility of exercising decisive influence over the business of an entity, including (i) access and user rights with respect to all or a portion of the assets of the relevant entity; and (ii) contractual and other rights that confer a decisive influence over the composition, deliberations or decisions of such entity’s corporate bodies.

Scope of Covered Investments

Under the Old Rules, the French prior authorization regime covered the following types of investments (the Covered Investments):

- the acquisition of control over a French company (the Control Test);
- the acquisition, in whole or in part, of a branch of business of a French company (the Asset Test); or
- for non-EU or non-EEA Foreign Investors, the acquisition of more than 33.33% of shares or voting rights (directly or indirectly) in a French company (the Threshold Test).

Under the New Rules, an investment by a non-EU or non-EEA investor qualifies as a Covered Investment under the Threshold Test if the Foreign Investor acquires, directly or indirectly, more than 25% of voting rights in a French company. The exemption

of European Foreign Investors from the Threshold Test applies only if the relevant chain of control does not include any non-EU or non-EEA Foreign Investors. The Control Test and Asset Test remain unchanged.

Affiliate Exemption

The 2019 Decree exempts certain transactions among affiliates from the prior authorization requirement. The exemption applies when:

- the foreign buyer and the seller are affiliates;
- the Foreign Investor crosses the 25% threshold (directly or indirectly) in a French company that is already under its control;² and
- the Foreign Investor acquires control (within the meaning of article L. 233-3 of the FCC) of a French company in which it had previously crossed the 25% threshold (directly or indirectly) pursuant to a foreign investment clearance delivered on the basis of the Threshold Test (the Minister may object to such acquisition of control within a 30-day period following notification thereof).

The “affiliate” exemption does not apply if the proposed investment has the effect of preventing the Foreign Investor from complying with commitments that were imposed on it in connection with a prior authorization, or if the purpose of the investment is to transfer abroad, wholly or partially, a branch of business falling within the scope of Covered Activities.

Extension of the Scope of Covered Activities

Under the Old Rules, the list of in-scope business activities (the Covered Activities) differed depending on whether the Foreign Investor was a European or non-European investor. The New Rules apply the same list of Covered Activities to all Foreign Investors. This will have implications for certain EU-sourced foreign investment flows in France.

The 2018 Decree extended the list of Covered Activities to space operations, storage of sensitive data and activities relating to certain key technologies, including R&D activities for semiconductors, artificial intelligence, cybersecurity, robotics, additive manufacturing, and dual-use goods and technologies.

The 2019 Decree has further extended the scope of French foreign investment control to written press and digital media involved in political or general news, agricultural activities involving national food security objectives, and R&D activities for certain critical technologies. The current list of critical

² The 2019 Decree provides that such control must have been acquired pursuant to a foreign investment clearance delivered on the basis of the Control Test.

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technologies includes quantum technologies and energy storage and may be further extended by ministerial order. This part of the reform brings the French foreign investment regime in line with the scope of the March 19, 2019, EU regulation for the screening of foreign direct investments into the Union (the EU Regulation).³

Enhancement of French Foreign Investment Process

Ruling Requests

Under the New Rules, a French company may submit a request to the Minister for a written opinion on whether or not the company's business activities fall within the scope of Covered Activities. The 2019 Decree also grants a Foreign Investor, acting in agreement with the relevant French company, the possibility to request a similar written opinion from the Minister. In the latter case, a copy of the Minister's opinion to the Foreign Investor must be provided to the French company.

The Order lists the required documents that the relevant Foreign Investor or French company must submit in the ruling request. As a matter of practice, in light of the required documents, which include, among others, a copy of all documents evidencing there is a proposed investment (*e.g.*, a letter of intent), the request for a ruling is a discretionary option that is available to the relevant Foreign Investor or French company only if there is a concrete investment proposal.

The Minister is required to provide an answer within two months of such request.

Applicants; Advanced Filings

The French prior authorization regime requires a Foreign Investor to file a request with, and obtain authorization from, the Minister prior to making a Covered Investment in a Covered Activity. The 2019 Decree clarifies that, when the investor's chain of control includes one or more Foreign Investors, any of them may submit the prior authorization request on behalf of the others. This clarification is particularly relevant for foreign private equity investors investing through their portfolio companies.

Additionally, pursuant to the Order, a Foreign Investor may submit a request for authorization before entering into a binding agreement with the target company and/or its owners. The Foreign Investor must provide documents evidencing the existence of a proposed investment that is sufficiently advanced. This particular reform has significant implications for the

M&A process. Until now, the practice was to file a request for authorization after the execution and announcement of a binding transaction. The New Rules allow Foreign Investors to file a request with French authorities at the outset of the process, similar to the Committee on Foreign Investment in the United States' (CFIUS) process.

Two-Step Review Process

The 2019 Decree has introduced a two-step review process — including a 30-business day Phase I review and, when necessary, a 45-business day Phase II review — that mirrors the U.S. CFIUS review system.

As part of the Phase I review, the Minister is required to make any of the following determinations:

- the proposed investment is out-of-scope;
- the proposed investment is in-scope and is authorized without any conditions; or
- the proposed investment is in-scope, and further examination (*i.e.*, Phase II review) is necessary to determine if French national interests can be protected by issuing the authorization subject to certain conditions, including the Foreign Investor entering into certain binding commitments vis-a-vis the French State.

If the Minister decides to launch a Phase II review, the Minister must, within 45 business days following the Foreign Investor's receipt of the Minister's Phase I decision, decide either to:

- reject the proposed investment; or
- issue an authorization subject to the Foreign Investor and its designated affiliate(s) entering into certain binding commitments vis-à-vis the French State.

If the Minister does not respond to the Foreign Investor within the allowable time during the Phase I or Phase II review process, the request is deemed rejected.

International Cooperation

The 2019 Decree states that the Minister may cooperate with international authorities to further investigate a prior authorization request and vet the accuracy of the information provided by a Foreign Investor, notably regarding the source of funding for the proposed transaction. Such cooperation is an important feature of many of the updated foreign investment regimes, including the European Union's foreign investment screening framework under the EU Regulation and FIRRMA in the United States.

³ Please see our client alert, "EU Adopts Regulation on Foreign Direct Investments" (July 1, 2019), for an overview of the EU Regulation.

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FIRRMA, in particular, included direction to the U.S. president to engage in international outreach to urge and help allies establish robust foreign investment screening processes and to facilitate coordination among the foreign investment screening apparatuses of allied nations. Further to this direction, in implementing FIRRMA, CFIUS has created a process whereby allied countries with strong foreign investment screening regimes may be considered for special “excepted investor” status.

Clarification of the Decision-Making Process

Conditional Authorization

The issuance of the French foreign investment clearance is generally subject to the Foreign Investor making certain commitments vis-a-vis the French state. The 2019 Decree provides that commitments imposed on Foreign Investors should be proportional to the preservation of French national interests and mainly seek to:

- guarantee the sustainability and security, on the national territory, of the relevant sensitive activities, notably by ensuring that such activities are not subject to foreign legislation that may affect their conduct;
- protect the relevant French entity’s proprietary know-how and expertise and block any attempt to gain access to it;
- adapt the internal organization and corporate governance of the relevant French entity and the terms for exercising the acquired rights in such entity; or
- grant access to information to the French competent authorities.

Under the 2019 Decree, the Minister may authorize the proposed transaction subject to the sale of part of the shares acquired in the relevant French company, or the sale of all or part of its sensitive assets or activities, to a third party approved by the Minister.

Additionally, the 2019 Decree provides that when an authorization is subject to certain conditions, the authorization must designate, within the persons comprising the chain of control of the relevant Foreign Investor, the person(s) responsible for complying with such conditions. In practice, the Minister will particularly focus on the person(s) who exercises real influence on the relevant French company.

Modification of Binding Commitments

Under the New Rules, a Foreign Investor may submit a request to the Minister to modify any ongoing binding commitments under

certain circumstances.⁴ The Foreign Investor must submit the necessary documents or other supporting information evidencing the relevant change of circumstance. The Minister is required to notify his decision to the Foreign Investor within a 45-business day period after receiving the request. If the Minister does not respond to the Foreign Investor within this time period, the request is deemed rejected.

The 2019 Decree also authorizes the Minister to modify any ongoing commitments binding upon a Foreign Investor on his own initiative, while respecting the principle of proportionality, under the relevant circumstances. The Minister must notify the Foreign Investor of his decision to modify any existing binding commitments, specify the reasons of his decision and grant the Foreign Investor a 45-business day window to submit comments. At the end of this period, the Minister will notify the Foreign Investor of the revised binding commitments and the date on which they must take effect.

The Minister’s Decision

The Minister may deny a prior authorization request if he determines that applying the conditions set forth by the 2019 Decree are not in and of themselves sufficient to ensure the preservation of French national interests.

Additionally, the Minister may reject the request for authorization for any of the following reasons:

- if there is a serious presumption that the Foreign Investor is likely to commit an offence or conceal an offence (“covered offence”);⁵
- if the Foreign Investor was convicted by a final judgment for a covered offence, or the equivalent of a covered offence pursuant to the law of any foreign jurisdiction, during the five years preceding the filing of the request for authorization; or
- if the Foreign Investor was sanctioned for breach of French foreign investment rules, or if the Foreign Investor has disregarded, in a serious and persistent manner, the Minister’s injunctive or protective measures, during the five years preceding the filing of the request for authorization.

Largely consistent with global regulatory trends, the factors outlined above signal that the French authorities will specifically take into consideration the track record and business ethics of

⁴ These circumstances include: (1) in the event of an unforeseeable change in the economic and regulatory environment of the French company’s sensitive activities; (2) when there is a change in the shareholding structure of the French company; and (3) when such modification was contemplated by the terms of the commitments that were agreed upon in the initial authorization.

⁵ The 2019 Decree provides a list of the relevant offences in the French Criminal Code and the French Tax Code.

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the Foreign Investor. In the same vein, the 2019 Decree requires the Foreign Investor to disclose any relationships with foreign countries or foreign public entities. The Minister may take into consideration such relationships in his decision.

The 2019 Decree requires the Minister to issue a reasoned decision for any refusal.

Sanctions and Remedies

The PACTE Law has given the Minister clearer and broader remedial powers to enforce compliance with French foreign investment rules and Foreign Investors' commitments:

- If a Foreign Investor does not submit a Covered Investment for authorization, the Minister may enjoin the investor to request authorization ex post or modify or unwind the transaction at the investor's expense.
 - If, after completion of the investment, the Foreign Investor fails to comply with its commitments, the Minister may, among other actions, withdraw the initial authorization (in which case the investor must request a new authorization or unwind the transaction) and impose new binding commitments on the investor.
- In certain circumstances involving the preservation of national interests, the Minister is entitled to (1) suspend voting rights and dividend distributions with respect to a portion of the French company's shares held by a Foreign Investor, (2) appoint a special trustee in charge of preserving national interests at the French company level and (3) restrict the Foreign Investor's ability to dispose of sensitive French assets.

The 2019 Decree further clarifies the Minister's enforcement powers. Notably, the Minister is required to issue a formal notice to the Foreign Investor and allow him to submit comments by a short deadline that must not be less than five days. At the end of the deadline, the Minister is required to notify the Foreign Investor of his decision and specify the timeline for the Foreign Investor to comply. The Minister may impose daily penalties ("*astreintes*"), of a maximum amount of €50,000 per day, on the Foreign Investor for noncompliance.

The Minister also may order a divestiture of all or part of the shares held by the Foreign Investor in the French company or all or part of the sensitive activities performed by such company to a third party.

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