

M&A: Draft German Law Gives More Teeth to FDI Controls – Reduces Deal Certainty – Imposes Broader Stand-still Obligations – Restricts Technical Due Diligence

Draft German investment control rules give the German government broader powers to intervene against M&A deals perceived to affect German (or EU) security or other public interests. New stand-still obligations will limit exchange of technical information prior to FDI clearance and affect deal timelines in wider business sectors. German FDI clearance needs to get early on higher priority in deal planning than under current practice.

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The draft amendments to the Foreign Trade Act (“AWG”) have just been submitted to Parliament (DS 19/18700 dated 21 April 2020). While details may change during the legislative discussions expected to be concluded in the summer 2020, it is important to keep this development on the radar for the planning of M&A deals that have German target elements. Main new elements of the FDI control regime are summarised below.

Broader review standard with lower intervention threshold:

- The government will have the right to issue a prohibition order or otherwise intervene already where a deal “is likely to have a negative impact on” German public order or security interests; whereas the current review standard requires an actual “danger” to public order and security.
- EU and other EU member states public interests may be taken into account likewise to justify intervention. There will be a cooperation procedure within EU, to be detailed in implementing regulations.
- The new review standard gives the government much more flexibility in its decision-making process and significantly increases deal uncertainty.

Extended stand-still sectors list:

Stand-still obligations until clearance will apply to all deals that must be notified for FDI clearance (previously only to defence related businesses). Thus, the stand-still obligations list includes deals with German target elements (as a rule 10% control trigger) in the following sectors:

- defence
- IT security (encryption, etc.)
- critical infrastructure (primarily relating to supply of water, food, health care, energy, transport, finance and insurance)
- specialised software for critical infrastructure
- large cloud computing
- telecommunications surveillance and telematics
- influential media businesses
- critical technologies (as contemplated by the EU FDI Screening Regulation)
 - critical technologies will be added and defined in separate implementing regulations (“AWV”);
 - according to Ministry announcements, initially that category will likely cover artificial intelligence, robotics, semiconductors, biotechnology, quantum technology;
 - this is potentially a broad category, as the government can easily amend the list to react to changing technology business landscape.

The stand-still obligations for the above sectors mean that until the government has cleared the deal (or is deemed to have cleared the deal)

- closing actions are invalid;
- the law expressly prohibits to give the buyer voting, dividend or equivalent rights; and
- confidential information relating to public order and security interests must not be made available to buyer (new requirement).

According to the legislative materials and contrary to the very broad wording of the draft law, the latter new requirement is not intended to hinder **due diligence** on commercial and general corporate matters. Lawmakers expressed an expectation that the information concerned would normally anyway only be shared after closing. However, that seems not realistic in all cases. In practice, parties will have to consider whether the law may hinder meaningful technical due diligence prior to FDI clearance. Due diligence on publicly available information such as patent or patent applications is not affected. Due to criminal law exposure, parties should exercise special caution in this respect. Non-compliance with the stand-still obligations is subject to criminal sanctions that include fines and up to 5 years imprisonment.

Government as a rule has 3 months review time as from the date it has received a complete notification; the question of completeness is not clearly defined by law and often results in delays as the authorities may request additional information before assuming a complete filing.

Deal planning and practice will have to reflect and accommodate the new regulatory parameters. Deal certainty will suffer due to the intrinsic vagaries of the lowered intervention threshold. Moreover, the limits on timely access to sensible information may induce buyers to push for additional closing conditions or other deal stop mechanisms or amendment rights in the event that post-clearance access to technical information reveals that information not to be in line with buyer expectations.

Details of the amended FDI regime remain to be seen as and when the new rules are being finalised.