EU Calls on Member States to Protect Health Care Sector from Foreign Takeovers

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On March 25, the European Commission ("Commission") issued Guidance to the Member States on the application of Regulation 2019/452 providing a framework for the screening of foreign direct investment (FDI) in the EU, and on restrictions on free movement of capital from third countries. The Guidance points out that the economic crisis brought about by the COVID-19 outbreak is posing increased risks to the healthcare sector and, more generally, to the EU's strategic capacities. In particular, the Commission warns that European strategic healthcare assets, such as medical or protective equipment and medical research establishments, might be subject to hostile takeovers through FDI. Moreover, the Commission advises Member States to be wary of potential "predatory buying" by foreign investors of strategic assets that might be affected by stock market volatility because of the pandemic.

1. Foreign Direct Investment Screening

The FDI Screening Regulation, which will fully enter into force in October 2020, provides a framework to enhance coordination and cooperation between Member States and the Commission in national cases involving the review of FDI on grounds of security and public order. Member States have the discretion to maintain their existing screening mechanisms, adopt new ones or remain without such mechanisms. Since Member States have exclusive competence to decide on matters related to national security and public order, they also retain the power to block or impose conditions on FDI in their respective territories. (For more information, see our EU Chapter in the ICLG Guide to Foreign Direct Investment Regimes)

In its new Guidance, the Commission reminds Member States that risks to critical health infrastructures and supply of critical inputs are explicitly included in the Regulation as factors to be considered when screening FDI. This essentially means that the consequences brought about by COVID-19 to public health can be invoked by Member States as compelling reasons of security and public order in the assessment of FDI. In this context, the Commission urges Member States to:

- Use their existing national screening mechanisms in order to address potential risks related to the healthcare industry and other critical sectors; or

- In case they do not currently have screening mechanisms, to set up such mechanisms and have recourse to other available tools to address risks to security or public order brought about by FDI.

In terms of procedure, the Commission refers to the following tools already provided under the framework for FDI screening:

- Member States, other than the one where the investment takes place, can require information and provide comments on the effects of the investment on their territories and on the European internal market as a whole.

- The Commission can also issue opinions addressed to the Member State in which the FDI is planned or has been completed, in particular when there is a risk that the investment affects projects of EU interest, such as Horizon 2020 projects related to the health sector.

- In cases where an FDI does not undergo national screening, Member States and the Commission have 15 months upon the completion of the investment to provide their comments. This in practice means that investments completed in March 2020 can be subject to comments until June 2021 and, as a result, potentially face *ex post* mitigating measures.

Finally, the Commission clarifies that the application of the screening framework is not subject to any thresholds and applies to all economic sectors (including to start-ups and SMEs).

2. Restrictions on free movement of capital from third countries

The EU Treaties provide for the free movement of capital not only between EU countries but also with third (non-EU) countries. However, Member States are allowed to derogate from this rule and impose restrictions on free movement of capital with third countries in order to attain public policy objectives. Such restrictions need to be suitable, necessary and proportionate. In its Guidance, the Commission recalls that public security and public health are considered by the case law as such objectives given that they promote society's fundamental interests.

According to the Commission, Member States can impose restrictions to capital movements from third countries, provided that there are legitimate overriding reasons of general interest, such as consumer and public health protection, financial stability and other public policy considerations, in the cases mentioned below:

- For investments that do not constitute FDI, namely investments that do not grant investors influence over management and control of a company (so called "portfolio investments"). Such investments may merit review in case the acquired shareholding confers rights that can be relevant for reasons of security and public order.

- Investments by third country investors that essentially qualify as "predatory buying" of strategic assets and aim at limiting supply in the EU territory. Potentially justifiable restrictions in such cases include measures ensuring security of supply or the provision of public services. This is subject to the proviso that less restrictive measures are not sufficient.

- For foreign investments in companies that are undervalued ("well below their true or intrinsic value") as a result of the economic impact of the pandemic, the Guidance indicates that restrictions could be imposed to safeguard public interest objectives.

Takeaways

The Guidance follows the approach that the Commission and the Member States have been adhering to in the past months in terms of increasingly strengthening FDI screening in order to safeguard growth within the EU. But this is the first time that the Commission has openly "called upon" Member States without screening mechanisms to set up "full-fledged" mechanisms in order to address healthcare-related risks and risks affecting the supply of critical inputs.

The main objective of the Commission seemingly is to disincentivize foreign investors from investing in EU companies whose activities are specifically linked to the sectors that have been affected by the pandemic. For this purpose, the Guidance is encouraging broader interpretations, on the one hand, of the grounds of national security and public order for FDI screening, and, on the other hand, of what might constitute justifiable restrictions to the free movement of capital.

We advise foreign investors planning to invest in EU companies (especially those connected with or affected by the pandemic) either by acquiring control, or through noncontrolling investments, to carefully assess the possibility that their investment might be subject to national intervention which could potentially lead to the adoption of commitments or, in a worst case scenario, to the prohibition of the investment.

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