JONES DAY

COMMENTARY

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Germany Blocks Two Transactions Involving Chinese Investors on National Security Grounds

IN SHORT

The Situation: Germany prevented State Grid Corporation of China ("SGCC") from acquiring a 20 percent minority stake in 50Hertz, one of Germany's four providers of high-voltage transmission systems, as well as the acquisition of a German specialist in high-strength metal forming by a French/Chinese consortium.

The Reason: Both transactions were prevented based on concerns of risk to public order and national security.

Looking Ahead: Other countries around the world are taking steps to adopt new, or amend existing, foreign direct investment review regimes to protect national security.

In what appears to be a coincidence with respect to the timing, Germany's government ("Government") effectively blocked two transactions involving Chinese investors on grounds of national security within days of one another. Such actions come at a time when Chinese investments in other jurisdictions also are being increasingly scrutinized, for instance by the Committee on Foreign Investment in the United States ("CFIUS").

On July 27, 2018, Kreditanstalt für Wiederaufbau ("KfW"), a German state-owned development bank, announced that it would acquire a 20 percent minority stake in 50Hertz, a Berlin-based company running a high-voltage transmission grid in Germany, from IFM Investors. According to the German Ministry of Economic Affairs and Energy ("BMWi"), KfW became active to prevent SGCC, a Chinese state-owned utility, from acquiring the 20 percent minority stake. The BMWi justified the decision on grounds of national security, arguing that 50Hertz is an important transmission system operator in Germany and responsible for the electricity supply to approximately 20 percent of the German population. SGCC's acquisition of the minority stake in 50Hertz could not have been blocked pursuant to Germany's foreign direct investment screening regulation ("AWV") because the AWV catches only the acquisition of 25 percent or more of the voting rights in a German company.

SGCC had tried to buy another 20 percent stake in 50Hertz from IFM Investors earlier this year. Ultimately, however, Elia, the operator of Belgium's electrical grid and the other shareholder of 50Hertz, acquired the stake (allegedly upon the request of the Government).

In light of the experience in the 50Hertz case, Germany will lower the threshold for catching transactions under the AWV from 25 percent to 15 percent of the voting rights in a German company by the end of this year.

Further, on August 1, 2018, a consortium of France's Manoir Group and China's Yantai Taihai Group abandoned the acquisition of Leifeld Metal Spinning, a German "*Mittelstand*" company with approximately 200 employees ("Leifeld") moments before the Government was set to issue its first formal prohibition order pursuant to the AWV. Leifeld is said to have special expertise in forming high-strength materials used in the aerospace and nuclear industries. According to press reports, the BMWi has been empowered to block the transaction if still necessary to protect Germany's public order and security, such as if the parties do not actually abandon the transaction.

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While the AWV has allowed the Government to block transactions on grounds of national security since 2004, the Government has never had to issue a formal prohibition order. In the past, parties voluntarily abandoned the transaction to avoid publicity once the Government raised concerns.

The two cases should not be deemed to reflect a protectionist approach vis-à-vis Chinese investments in Germany. Recently, BMW and Daimler signed cooperation agreements with Chinese original equipment manufacturers ("OEMs") regarding the development of autonomous vehicles (requiring the exchange of sensitive information) during meetings between the governments of China and Germany. Further, a number of other Chinese investments in German companies apparently enabled the companies to expand their business, in particular in China, and did not lead to a drain of expertise and jobs feared by some in Germany.

Further, China's Ningbo Jifeng's recent takeover offer for German automotive supplier Grammer received a warm welcome by German automotive OEMs and politicians alike. Instead, the two cases indicate that the Government performs a detailed review of the potential risks of a given transaction to Germany's security and public order. Interested parties are therefore well advised to carefully assess their individual transaction and, depending on the circumstances, to expect longer review periods.

In addition, the two cases are likely to reignite the discussion on the draft EU Regulation Establishing a Framework for the Screening of Foreign Direct Investments into the European Union. The European Union has identified the investment screening proposal as a legislative priority and aims to adopt the Regulation by the end of the year.

Many countries around the world are taking steps to adopt new, or amend existing, foreign direct investment review regimes to, among others, protect national security. For example, the United States is expected to change CFIUS and its foreign direct investment regime shortly. China and the United Kingdom are also revamping their foreign direct investment regimes.

THREE KEY TAKEAWAYS

1. Citing national security concerns, Germany recently prevented two acquisitions of German companies by Chinese investors.

2. Despite these recent developments, Germany does not take a protectionist approach to inbound investments from China.

3. The German goverment carefully evaluates the potential risks of a given transaction to Germany's national security, and thus potential investors should allow time for lengthy review periods.


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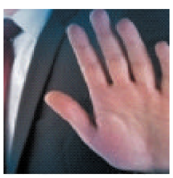

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