Matheson

Response to Public Consultation on Investment Screening

22 May 2020

In this response to the Department of Business, Enterprise and Innovation's ("**DBEI**") public consultation on foreign investment screening ("**Response**"), we set out below our perspectives on the *design* of any investment screening mechanism that may be introduced.

At the outset, it is important to note that we welcome the statement by Minister Humphreys that it is important that any future Irish investment screening mechanism "*balances Ireland's continued attractiveness as a location for inward investment, with a robust, but proportionate Investment Screening Mechanism that protects security and public order*".[1] We would be concerned if an investment screening mechanism were introduced which imposed a disproportionate burden on businesses and impeded investment in Ireland.

This Response does not purport to express any views on the *need* for any future investment screening mechanism, which is ultimately a policy decision for Government. The focus of the Response is therefore on the *design* of any investment screening mechanism, where a decision is made to introduce such mechanism, and on highlighting technical and practical issues relevant to this.

Based on our experience, the introduction of any investment screening regime would raise many complex issues and lessons can be learned from the experience of existing review processes. Accordingly, we have outlined below some of these issues and potential sources of guidance. In doing so, we have drawn upon our experience of advising on matters requiring merger control approval, including pursuant to the Irish CCPC and DCCAE regimes, the regime under the EU Merger Regulation ("**EUMR**"), and international FDI regimes which our team is familiar with arising from our extensive international experience in this area.

This Response assumes that any new mechanism would fall within the scope of what is envisaged by EU Regulation 2019/452 establishing a framework for the screening of foreign direct investments into the EU ("**EU Investment Screening Regulation**"), and in particular would centre around the EU law objective of safeguarding national security and public order.

Finally, as a general remark, we would suggest that, where relevant and to the extent possible, there are legal certainty benefits to any new investment screening regime using legal concepts which are well understood from existing merger control legislation. For example, relevant concepts from the Competition Act 2002 (as amended) ("**CA02**") which may be transferable include: (i) an "undertaking", and (ii) approval powers such as the power to authorise, apply conditions or prohibit transactions.

---

1. See https://dbei.gov.ie/en/News-And-Events/Department-News/2020/April/24042020.html.

1 The "scope" of any future investment screening regime

The key considerations in relation to the jurisdictional scope of any future mandatory investment screening regime include (1) defining the trigger event, for example in terms of the acquisition of "control" or "significant influence" over certain businesses; (2) defining the sub-set of businesses or business sectors that may present a national security risk; (3) designing a jurisdictional / size threshold; and (4) considering the choice between a mandatory and a voluntary / "call-in" regime. We have set out more detail on these considerations below.

- *Defining the trigger event* – We note that a policy decision will ultimately need to be taken as to what level of interest by a third country investor is likely to represent a sufficiently material national security risk to warrant application of the regime. However, the below considerations could be taken into account in weighing up the various options.

  - *Object of trigger event* – as the definition of "Foreign Direct Investment" in the EU Investment Screening Regulation is extremely broad, an important issue is what type of 'target' will any new Irish regime capture, and in particular if and when will it capture acquisitions of interests in assets (rather than legal entities). In this regard, we would see legal certainty benefits to defining the trigger event by reference to the competition law concept of "undertaking" and the EUMR Jurisdictional Notice guidance on when asset acquisitions are captured by the EUMR (ie, when assets constitute a business with a market presence to which a market turnover can be clearly attributed). While the EU Investment Screening Regulation anticipates that jurisdiction might be taken over investments in 'start-ups' or technologies 'in development', we do not anticipate that use of the aforementioned established legal concepts would limit jurisdiction to an extent which is problematic from a Government policy perspective.

  - *Nature of trigger event - "control"* – the relevant trigger event for any future investment screening regime could be based on the acquisition of "control". The concept of "control" is well established under the Irish and EU competition law merger control regimes, as the possibility of exercising "decisive influence", which can be established either on a legal/contractual (ie, *de jure*) or factual (ie, *de facto*) basis.[2] Use of such definition would enhance legal certainty due to the benefit of there being extensive interpretation of the EU law concept of "control" in EU case law, the European Commission's guidance documents and the decisional practice of both the European Commission and the Irish CCPC (and its predecessor).[3]

  - *Nature of trigger event - "significant" or "material" influence* – the ability to exert "significant" or "material" influence over the target business's commercial behaviour or strategy could be proposed to be a sufficient trigger event like under the UK merger

2. See section 16(2) of the Competition Act 2002 (as amended) and Article 3(2) EUMR.

3. In particular, see paragraphs 11 onwards of the European Commission's Consolidated Jurisdictional Notice which reflects the key principles set out in the relevant EU case law and also summarises the European Commission's further guidance on specific practice points.

control regime (as established by the UK Enterprise Act 2002). Since this is a less familiar concept from an Irish and EU law perspective, one potential downside of adopting this concept from both a regulatory as well as an industry perspective would be reduced certainty due to the lack of any clear EU or Irish law precedent, guidance or decisional practice.

  - *Percentage threshold* – the trigger event for any future investment screening regime might refer to a particular level of shareholding, voting rights, board seats or assets of the target business that are set to be acquired. Whilst percentage thresholds have been established in a number of the FDI regimes across the EU (eg, France, Germany, Spain), we understand the experience is that such thresholds (especially where they are set at a low level) can apply in a potentially crude manner that results in over-regulation. In the Irish context, we note that there is a percentage threshold in the definition of "significant influence" under the Irish media merger regime (which is relevant to the substantive test but not the jurisdictional test) and we have experience of it being interpreted in a manner which results in very remote minority shareholdings (ie, indirect, at several levels removed from the relevant business) being taken into account without there being a clear need for this.

  - *"Hybrid" model* – any future regime could incorporate one or more of the above trigger events, like the UK merger control regime where the concept of "control" (ie, "*ceasing to be distinct*" under section 26 of the UK Enterprise Act 2002) covers both "control" (legal/contractual (ie, *de jure*) and factual (ie, *de facto*)) and "material influence" (as per the above description). This hybrid approach may tend to increase complexity and reduce predictability, however.

- *Defining the types of businesses or sectors that present a national security risk*

  - For the purposes of this Response, we have assumed that the list of sectors that are set out in Article 4(1) of the EU Investment Screening Regulation will serve as a reference point for any future Irish investment screening regime. Since the list of sectors under Article 4(1) is very broad in scope, it is difficult to envisage any additional sectors (if any) needing to be added to this list because of their likely national security implications. Clearly, the issue of legal certainty as regards whether a transaction is to fall within the scope of a regime will be key.

  - We would also note that the very broad scope of the some of the definitions in Article 4(1) of the EU Investment Screening Regulation – in particular the potentially broad definitions of "*critical infrastructure*", "*supply of critical inputs*" and "*access to sensitive information*" (noting what these are said to "include") – will have implications for the design of the regime (ie, a mandatory as compared with a voluntary or "call in" regime). In particular, a mandatory regime, could result in a wide and conservative interpretation of such definitions being taken by both (i) businesses – to avoid any sanctions for non-compliance with notification requirements – and (ii) the Minister / regulator – to avoid creating a "no jurisdiction" precedent - thus increasing the

regulatory burden on both sides. This has been our experience as regards the approach to the broad definition of "media business" under section 28A CA02 for the purposes of the mandatory Irish media merger regime administered by the DCCAE.

- Overall, definitions of sectors subject to any new regime must balance the objectives of (i) enabling adequate and agile regulation in the long-run, and (ii) avoiding over-regulation. At a minimum, we would recommend that detailed guidance is issued in relation to the types of businesses that would come within each definition in order to increase legal certainty and avoid unnecessary notifications or burdens.

- *Designing the jurisdictional threshold* – two key (and somewhat related) considerations for the design of the jurisdictional threshold for any future investment screening regime are (i) whether the test will be focused on the activities of the target in the State, and (ii) whether the test will incorporate any minimum financial thresholds for jurisdiction to arise.

  - Focus on the activities of the *target business* in the State – the question here is whether the jurisdictional test will require the target business to have a minimum level and type of activity in the State for jurisdiction to arise. The approach under the Irish media merger regime is of relevance in this regard. Under this regime, provided the transaction involves two parties that carry on a "*media business*" as defined under section 28A CA02 (ie, anywhere in the world), only one of the parties (which could be merely the acquiring party) then needs to "*carr*[y] *on a media business <u>in the State</u>*". Furthermore, the media merger regime applies as long as two media businesses are concerned and regardless of whether the target / subject matter of the transaction is a media business. Based on our experience, this can lead to unanticipated situations where a mandatory media merger notification arises even where (i) only the acquiring party (and not the target) is active in the State, and (ii) the target is not a media business. We would therefore recommend that consideration be given to ensuring that the jurisdictional test for any future investment screening regime requires that the *target* has a minimum level of activity in a relevant sector, and a sufficient nexus to, the State. This threshold could potentially be modelled on the "*carry on business in the State*" requirement under the Irish media merger regime.

  - *Minimum financial thresholds* – relatedly, the question arises whether the jurisdictional test should incorporate minimum financial thresholds. Such financial thresholds would require both the acquiring party and the target business to have a minimum level of activity in, and therefore a sufficient nexus to, the State. In this regard, we would note that even the new national security provisions that came into force in the UK in June 2018 in relation to businesses active in the supply of military or dual-use goods, computing hardware or quantum technology require the target to have generated €1 million in the UK (or otherwise have a 25% share of supply in the relevant sector). To the extent that DBEI wishes to consider financial metrics other than turnover, we would encourage it to refer to the large body of research and public debate on proposals to include a 'transaction value' threshold in the competition merger control

jurisdiction tests at EU level and decisions to do so in a number of Member States including Germany and Austria.

- *Mandatory v voluntary / "call-in" regime -*

  - A key question in relation to the design of the regime will be whether it will be *mandatory* in terms of requiring businesses to notify before completion or *voluntary* in terms of allowing the reviewing body to "call in" a transaction for review where it perceives a national security risk (even where the transaction has been completed).

    Where a mandatory *notification* requirement is introduced, the regime would not necessarily need to (i) be "suspensive" in terms of requiring that the transaction is not completed until approval is granted, or (ii) automatically result in a detailed substantive review and decision by the reviewing body. In relation to (ii), DBEI might consider avoiding this through a "light touch mandatory regime". This option could simply involve the mandatory submission of basic transaction details (eg, in a one-page form), in response to which the reviewing body would be required to decide whether or not to open a substantive review (leading to a reasoned decision) within a defined time period (eg, up to 10-15 working days). This option could potentially remove the burdens of (i) market surveillance and detailed review/decision preparation for 'no issues cases' from the reviewing body and (ii) a detailed notification and delay from transaction parties to 'no issues cases'. It is our experience that some 'no issues cases' tend to be captured by mandatory regimes, no matter how a jurisdictional test is structured.

  - Where a voluntary regime is introduced allowing the reviewing body to "call in" a transaction for review within a fixed time period, consideration would need to be given to whether the reviewing body would be equipped with a market surveillance function to identify transactions that may present national security issues and the resource implications that this may entail. A mechanism allowing transaction parties to provide the reviewing body with basic details in relation to their transaction (similar to what is mentioned above as an option for a "light touch mandatory regime") could also be considered in a voluntary regime. This would provide the reviewing body with much needed market intelligence and give the transaction parties some legal certainty as to whether their transaction will be reviewed (noting the UK Competition and Market Authority's practice of accepting informal briefing memoranda to be submitted in relation to live transactions). One further consideration is that, in a voluntary regime which allows transactions to proceed to completion without notification, the reviewing body would need heavy unwinding powers if it ultimately were to decide that the completed transaction presents a sufficiently material national security risk and should be prohibited. While this is arguably an unlikely scenario, the lack of experience in exercising such heavy unwinding powers in any of the current Irish regulatory regimes would need to be taken into account.

2 The procedural and substantive "workings" of any future investment screening regime

By way of introduction to this point, the key considerations in relation to the procedural and substantive "workings" of any future investment screening regime include (1) considerations in relation to the appropriate reviewing body and expertise available; (2) defining the substantive test for reviewing transactions; (3) whether any new regime should run parallel with, or consecutive to, other review processes; and (4) the scope of enforcement powers that are vested in the reviewing body. We have set out more detail on these considerations below.

- *Considerations in relation to the appropriate reviewing body* and expertise available – a key question is clearly who will be the decision maker in any new regime, whether it will be a Government Minister or an independent body and related resourcing and expertise available to such decision maker. We understand that the Consultation envisages that a Government Minister will be empowered to make a decision on the issues. As a relatively small EU Member State, resourcing is an important practical issue which may dictate that Ireland follow a slightly different approach to larger Member States. In particular, we note that where Ministerial decision making is decided upon, external expertise may be necessary. However, care would need to ensure the availability of such expertise to avoid that resourcing giving rise to delay and uncertainty, in particular where the external expertise is engaged on an *ad hoc* / case-by-case basis. There is a clear need for speed and consistency in order to minimise the overall regulatory burden on business, and in particular the timing impact on live deals. Overall, Ministerial decision-making needs to be supported with dedicated resources within the DBEI and calling on external expertise efficiently.

- *Whether any new regime should run parallel with, or consecutive to, other review processes* – one of the key procedural questions is whether any future investment screening regime would run in parallel with, or consecutive to, a merger control review control review by the CCPC or the European Commission in particular. In this regard, it should be noted that the Irish media merger regime runs consecutive to the Irish (or EU) competition merger control regime, in that the Minister for Communications only commences its separate media merger review once the CCPC or the European Commission have completed their merger control review. This can lead to considerable timing delays and difficulties for merging parties which are arguably unnecessary, in particular in 'no issues' cases where the competition law approval decision does not contain information which is of clear relevance to the decision to be taken by the Minister for Communications. Accordingly, it is our view that any new regime should run in parallel to other review processes and we regard this as appropriate from the regulator's perspective also given that the policy concerns / substantive test(s) from a national security perspective are very different to other concerns / tests such as in relation to competition law.

- *Defining the substantive test for reviewing transactions* –

  - *Whether to define "national security risk"* – for the purposes of this Response we have assumed that the substantive test under any new FDI regime would be based on the test that has been introduced by the EU Regulation, namely whether the transaction

"*is likely to affect public order and security*". From experience, we believe it would be unnecessary, and possibly even confusing, to introduce an additional substantive test for reviewing transactions under any new regime that differs from the substantive test that would need to be applied for the purposes of ensuring the State's compliance with the cooperation and information sharing mechanisms under the EU Regulation. We believe the definition of when a transaction "*is likely to affect security or public order*" should also follow the approach under the EU Regulation which sets out the types of activities of the target business (Article 4(1)) and the relevant considerations regarding the acquiring business (Article 4(2)) that may be likely to affect security or public order. This "halfway house" approach – ie, where the definition is stated to include certain types of activities, rather than being stated in an exhaustive manner – is consistent with the approach to the definition of the substantive test under the Irish media merger regime where the "*plurality of the media*" under CA02 is stated to include "*both diversity of ownership and diversity of content*" without being stated in an exhaustive manner.

  - *Separate consideration of different national security risks* – relatedly, we believe there would be merit in defining the substantive test in a way that requires separate consideration of the different types of national security risks, namely the target risk (ie, based on the nature of the activities of the target business), the acquirer risk (ie, based on the links or activities of the acquiring business) and the "trigger event" risk (ie, based on the level of control or influence being acquired). This would be consistent with the approach under Article 4 of the EU Regulation and also the approach that has been proposed in the UK.[4]

- *The scope of approval powers that are vested in the reviewing body* – as a general matter, approval powers such as the power to authorise, apply conditions or prohibit transactions should be borrowed from the Irish CCPC and DCCAE regimes in particular given the familiarity with those concepts and the body of practice that has been built up within these existing regimes. As regards the scope of any powers to apply conditions, it should be specifically provided for that these may only be exercised to address concerns which are (i) national security-specific (ie, not motivated by wider public interest considerations), and (ii) transaction-specific (ie, not pre-existing or inevitable).

3 Conclusion

We hope this Response assists DBEI in identifying issues and options to consider in ensuring that any new regime is both effective and proportionate, consistent with Minister Humphrey's objective to ensure "*Ireland's continued attractiveness as a location for inward investment*". We trust that the DBEI will continue to consult with stakeholders as policy-making and legislative drafting evolves, noting that it is difficult for stakeholders to submit detailed views at this early stage. Please let us know if you would like further information on any of the points we have raised.

[4] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/728311/20180717_Statement_of_policy_intent_-_shared_with_comms.pdf