

COVID-19. EXTRAORDINARY MEASURES IN SPAIN SUSPENSION OF FOREIGN INVESTMENT FREEDOM

Among the extraordinary measures adopted by the Spanish authorities to deal with the Covid-19 outbreak (which includes the official declaration of the State of Alarm throughout the whole national territory¹), the Spanish Government has approved the Royal Decree-Law 8/2020 on urgent extraordinary measures to confront the economic and social impact of the COVID-19 outbreak (RD-L 8/2020), which is in force as from 18th March.

The measures included in this new legislation are of very different nature and responding to different concerns. The **purpose of this Legal Alert is limited to analyze** one of said measures, the **suspension of foreign investment freedom**.

The fourth final provision of RD-L 8/2020² suspends the foreign investment freedom and introduces *ex ante* mechanisms of control; it is based on the fact that the recent impact of the pandemic on the global stock markets creates the "*certain threat*" that foreign investors may acquire Spanish companies (listed and non-listed) whose value is being undermined, and intends to protect the Spanish companies active in strategic sectors before investors from outside the EU or the European Free Trade Association (EFTA).

The legal change consists in the modification of Law 19/2003, on the legal regime of capital movement and foreign economic transactions. Before getting into the detailed analysis of this new provision it should be highlighted that it creates important uncertainties regarding the scope of its effects; therefore, it is not fully clear which will be the extent and intensity of the practical impact of the measure.

The **main elements of this regime** are the following:

- Who are the foreign investors subject to this regime?

Any natural person or entity national of a third country (countries outside EU and EFTA).

Nevertheless a difference is made between (i) entities under the control of foreign state bodies or armed forces, or sovereign funds from third countries (along with those already involved in activities affecting security or public order in a Member State, and whether there is a serious risk that the foreign investor engages in illegal or criminal activities), and (ii) other foreign investors. For the latter the operations requiring *ex ante* authorization are limited to those related to critical sectors, for investors under (i) the requirement is irrespective of the activities of the Spanish target company.

A key point remains unclear for both types of foreign investors. Although the wording of the article "*direct foreign investment*" may lead to the understanding that the

¹ Royal Decree 463/2020, of March 14th, declaring the state of emergency for the management of the health crisis caused by COVID-19.

² Please find a translation into English Language of this provision in Annex.

operations carried out by Spanish (or EU or EFTA) subsidiaries of foreign investors are out of the scope of this regime, we understand such legal concept can be interpreted according to article 2 of the Regulation (EU) 2019/452³. Accordingly, operations carried out by entities under the (direct or indirect) control of foreign investors could be deemed to be within the scope of the new provision.

- What foreign investment operations are subject to this regime?

The analysis of this question requires a subjective and objective approach.

- Objective aspect (operations and critical sectors):

The operations subject to the new regime are those by which the foreign investor holds a stake equal or higher than 10% of the share capital of a Spanish company, or any other agreement, act or operation through which the foreign investor is effectively involved in the management or control of a Spanish company.

The sectors declared as critical for the purposes of this regime are those related to critical infrastructure, critical and dual use technologies, essential supplies, data and media. The inclusion of all the energy (power, gas, petrol) activities is made express and clear, so power generation, transmission, distribution, supply and trade are within the scope of this measure. The Government becomes entitled to include new sectors.

- Subjective aspects (investors and targets):

Alongside the uncertainty on the precise scope of the foreign investors subject to this regime, it remains unclear whether the target company that is indirectly (but not directly) involved in any critical sector is (or not) within the scope of the provision.

- Which is the applicable regime?

Save for those previously authorized by the Spanish Government, the foreign investments subject to this regime shall be null and void and considered an infringement. The Government is entitled to impose conditions to the operation, prohibit, unwind or authorized it. The application for the *ex-ante* authorization is deemed to be rejected ("*silencio negativo*") in case there is no decision by the Government within the legal term (six months as from application date⁴); as from then the foreign investor would be entitled to challenge the "decision" before the contentious administrative courts).

The infringement can be sanctioned with a fine amounting up to the total value of the operation.

³ Regulation (EU) 2019/452 of the European Parliament and of the Council, of 19 March 2019, establishing a framework for the screening of foreign direct investments into the Union: "foreign direct investment" means an investment of any kind by a foreign investor aiming to establish or to maintain lasting and direct links between the foreign investor and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity in a Member State, including investments which enable effective participation in the management or control of a company carrying out an economic activity. <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32019R0452&from=EN>

⁴ In accordance with article 10 of the Royal Decree 664/1999

- When shall expire the effectiveness of this regime?

The expiration of this regime requires a specific decision adopted by the Spanish Government and therefore is not directly linked to the end of the State of Alarm situation.

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Consequently, there are major uncertainties around the application of this new regime that affect key aspects of its objective and subjective scope and include (additionally to the ones previously remarked): whether operations to increase a previously held stake of 10% (or higher) or the incorporation of brand new subsidiaries are subject to the new regime; or whether previously agreed transactions are included in the scope of this provision (on this regard the specific structure of the transaction may be decisive, the same way that the specific agreements will require analysis for the purposes of deciding on the existence of involvement in the management or control over the Spanish company), etc.

For this purposes the declared aim of the measure and the provisions of EU Regulation 2019/452 are key elements for interpretation and lead to give the regime an ample scope; moreover please note that this provision somehow anticipates the application of the aforementioned EU Regulation (effective as from October 2020) and should be applied in accordance with the free trade Treaties in force subscribed by Spain and/or the EU with the corresponding third country.

Accordingly, any transaction involving investors from outside EU or EFTA will require to be analyzed from this point of view to determine whether the authorization from the Spanish Government is required to complete the deal.

ANNEX

Translation into English of Fourth Final provision of RD-L 8/2020.

Amendment of Law 19/2003, of 4 July, on the legal regime of capital movements and foreign economic transactions.

The Law 19/2003, of 4 July, on the legal regime of capital movements and foreign economic transactions is modified in the following terms.

One. *An Article 7 Bis is added with the following literal wording:*

"Article 7 Bis. Suspension of the liberalization regime of certain foreign direct investment in Spain.

1. For the purposes of this article, it is considered as a foreign direct investment in Spain any kind of investments made by residents from countries outside the European Union and the European Free Trade Association when the investor takes a stake equal or higher than 10% of the share capital of a Spanish company, or when as a result of the corporate operation, act or legal business which enable effective participation in the management or control of a company.

2. It is suspended the liberalization regime of foreign direct investments in Spain which are carried out in the sectors mentioned below and that affect the public order, public safety and public health.

Specifically, the sectors are the following:

(a) critical infrastructure, whether physical or virtual, including energy, transport, water, health, communications, media, data processing or storage, aerospace, defence, electoral or financial infrastructure, and sensitive facilities, as well as land and real estate crucial for the use of such infrastructure; understanding those referred to in Law 8/2011 of 28 April, which lays down measures for the protection of critical infrastructure.

(b) critical technologies and dual use items as defined in point 1 of Article 2 of Council Regulation (EC) No 428/2009 (15), including artificial intelligence, robotics, semiconductors, cybersecurity, aerospace, defence, energy storage, quantum and nuclear technologies as well as nanotechnologies and biotechnologies;

(c) Supply of critical inputs, in particular energy, including by those who are regulated by Law 24/2013 of 26 December, of the Electricity Sector, and in Law 34/1998 of 7 October on the Hydrocarbons, or those relating to raw materials, as well as food security.

(d) access to sensitive information, including personal data, or the ability to control such information, in accordance with the Law 3/2018, of 5 December, on Personal Data Protection and Guarantee of digital rights.

(e) Media.

3. The liberalization regime of the foreign direct investments in Spain is also suspended in the following cases:

(a) whether the foreign investor is directly or indirectly controlled by the government, including state bodies or armed forces, of a third country,, and for the purposes of determining the existence of such control, the criteria set out in Article 42 of the Commercial Code ("Código de Comercio").

(b) whether the foreign investor has already been involved in activities affecting security, public order and public health in another Member State, and in particular those listed in paragraph 2 of this article.

(c) whether proceedings, whether administrative or judicial, have been instituted against the foreign investor in another Member State or in the home State or in a third State for engaging in criminal or illegal activities.

4. The Government may suspend the liberalization regime of the foreign direct investments in Spain in those other sectors not contemplated in the paragraph 2 of this article, where they may affect public security, public order or public health, in accordance with the procedure laid down in Article 7 of this Law.

5. The suspension of the liberalization regime established in accordance with the paragraphs 2, 3 and 4 of this article shall determine the submission of such investment operations to obtain authorization, in accordance with the established in Article 6 of this Law.

Investment operations carried out without the required authorization shall be invalid and of no legal effect, until the legalization is obtained in accordance with the provisions of article 6 of the Law.

6. The suspension provided for in this article shall be in force until an agreement is reached on Council of Ministers ("Consejo de Ministros") determining its lifting."

Two. *Article 8(2) is amended and the literal wording would be as follows:*

"2. They shall constitute very serious infringements:

(a) The carrying out of prohibited acts, businesses, transactions or operations by virtue of the adoption of the measures referred to in Articles 4 and 5.

(b) The performance of acts, business, transactions or operations without request authorization where required under Articles 6, 7 and 7 Bis, or prior to granting it or with failure to comply with the conditions set in the authorization.

(c) The lack of veracity of applications for authorization submitted to competent bodies, in so far as it can be considered as relevant."

Three. *Article 12(2) is amended and the new literal wording would be as follows:*

"2. The competence to initiate and conduct sanctioning procedures resulting from the application of the regime provided for in the Law and for the imposition of the corresponding sanctions shall be governed by the next rules:

(a) The jurisdiction to initiate and conduct proceedings will be of the Secretary of the Commission for the Prevention of Anti Money Laundering and Monetary Infractions, except in matters of foreign direct investments in Spain, which will be the responsibility of the body designated by the holder of the General Directorate for International Trade and Investment ("Dirección General de Comercio Internacional e Inversiones").

(b) The imposition of penalties for very serious infringements shall be the responsibility of the Council of Ministers, on the proposal of the Minister of Economic Affairs and Digital Transformation.

However, in the case of very serious infringements in foreign direct investments in Spain, the imposition of sanctions will correspond to the Council of Ministers, based on the proposal of the Minister of Industry, Commerce and Tourism.

(c) The imposition of penalties for serious infringements shall be the responsibility of the holder of the Ministry of Economic Affairs and Digital Transformation, based on the proposal of the holder of the Secretary of State of Economy.

In the event of serious infringements in matters of foreign direct investment in Spain, the imposition of sanctions shall be the responsibility of the Minister of Industry, Trade and Tourism, based on the proposal of the Secretary of State of Commerce.

(d) The imposition of penalties for minor infringements shall be the responsibility of the owner of the General Directorate of the Treasury and Financial Policy, based on the proposal of the examining body.

In the case of minor infringements in the area of foreign direct investment in Spain, the imposition of sanctions shall be the responsibility of the holder of the General Directorate for International Trade and Investment, based on the proposal of the examining body."