China and Argentina: Foreign Direct Investment screening regulations in times of COVID-19

1. Introduction

As the second largest economic entity in the world, in the last couple of years China has made remarkable achievements in expanding the process of "Reform and Opening-up" to foreign investments and eliminating trade barriers. In turn, foreign direct investments ("FDI") have been central to the economic development of Argentina since the return to democracy in 1983, and notably within the privatization processes of public companies which started in 1989 and continued throughout the 1990's decade.

That said, in recent years, the intensity of the "National Security Review" that is conducted within the FDI screening mechanisms has been substantially enhanced. In August 2018, U.S. President Trump formally signed the *Foreign Investment Risk Review Modernization Act*, which further strengthened the national security review for foreign investment in the United States; then in March 2019, the European Union ("EU") adopted a regulation for the screening of foreign direct investments within the EU; more recently and amid the outbreak of COVID-19, Spain and Italy introduced changes to their national FDI screening mechanisms to better deal with the possible economic impact of the pandemic and to protect undervalued companies against hostile takeovers from abroad. Germany may also tighten its existing FDI screening mechanisms very soon to better protect certain critical sectors or companies.

With the influx of various kinds of foreign funds and capitals, the review of mergers and acquisitions ("M&A") of specific industries and companies concerning national security has gradually become a hot topic that is worthy of strict consideration.

2. Foreign Investment Law of the People's Republic of China

Effective 1 January 2020, the latest-revised *Foreign Investment Law of the People's Republic of China* ("*Foreign Investment Law*") clarifies that the State establishes a security review system for foreign investment, under which the security review shall be conducted for foreign investment affecting or likely affecting the state security (Article 35). This means that China has officially established a national security review system for foreign investment ("security review system") from the national law level.

The scope, standard and procedure of security review for M&A stem from documents issued by certain regulatory authorities[1]. According to article 9 of the *Provisions on Security Review of M&A,* M&A of

[1] For example, the Notice of the General Office of State Council on Establishment of Security Review System Pertaining to Mergers and Acquisitions of Domestic Enterprises by Foreign Investors issued in February 2011 ("Notice of Security Review of M&A") and Provisions of Ministry of Commerce on

domestic enterprises by foreign investors[2], shall be analysed on the basis of their substantial contents and actual impact, to determine whether they fall within the scope of the M&A security review.

The Notice of Security Review of M&A lays down that the material scope of the security review shall be: a) M&A of domestic enterprises and supporting enterprises involved in the military industry, enterprises located near key and sensitive military facilities, and other units related to national defence and security by foreign investors;

b) M&A of domestic enterprises involved in key agricultural products, key energy and resources, vital infrastructure, important transportation services, core technologies, significant equipment manufacturing, etc which are related to national security by foreign investors, in which the actual controlling rights of the enterprises may be obtained by foreign investors.

At the moment, the National Development and Reform Commission ("NDRC") undertakes the task of carrying out the security review for foreign investment. In addition, the State Council establishes a system of Inter-ministerial Conference for security review on M&A by foreign investors ("Inter-ministerial Conference") whose assessment take the following factories into account:

a) The impact of M&A on national defence and security, including the production capacity of domestic products, capacity for provision of domestic services and the relevant equipment and facilities required for national defence.

b) The impact of M&A on stable operation of national economy.

Implementation of Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors issued in August 2011 ("Provisions on Security Review of M&A").

[2] M&A of domestic enterprises by foreign investors shall comprise any of the following type of transactions:

a) A foreign investor purchases the equity of a domestic non-foreign investment enterprise or subscribes to the capital increase of a domestic non-foreign investment enterprise, such that the domestic enterprise is transformed into a foreign investment enterprise.

b) A foreign investor purchases the equity of the Chinese shareholder of a domestic foreign investment enterprise or subscribes to the capital increase of a domestic foreign investment enterprise.

c) A foreign investor establishes a foreign investment enterprise and agrees on purchasing the assets of a domestic enterprise and operating such assets through such foreign investment enterprise, or purchases the equity of a domestic enterprise through such foreign investment enterprise.

d) A foreign investor directly purchases the assets of a domestic enterprise and uses the assets to invest in the establishment of a foreign investment enterprise for operating such assets.

c) The impact of M&A on basic order of society.

d) The impact of M&A on research and development abilities of core technologies involving national security.

Apart from the above general framework, in April 2015 the General Office of the State Council issued *Notice of the General Office of State Council on Promulgation of the Trial Measures on National Security Review for Foreign Investments in Pilot Free Trade Zones*, according to which specific measures have been formulated in "Pilot Free Trade Zones" for piloting implementation of national security review measures for foreign investments.

3. Foreign Investment law of Argentina

The main law governing foreign investments in Argentina is Law No 21,382 ("FIL"), which was enacted in 1976. The law has since been considerably amended to liberalise the rules applicable to foreign investment. The Ministry of Economy is the ultimate overseer of foreign investment through its different Secretariats.

FIL established a legal regime aimed at promoting foreign investment in the country, based on the principle of non-discrimination in the treatment of national and foreign investors. In fact, the FIL lays down that foreign investors can make investments in the country destined to the promotion of activities of an economic nature, or to the expansion or improvement of existing ones, under the same conditions as investors domiciled in the country, having the same rights and obligations as the Constitution and the Laws accord to national investors, subject to the provisions of Law No. 21,382 and those contemplated in special or promotional regimes (art. 1).

Even foreign investors can use any of the legal forms of organization provided in the national legislation (art. 6 FIL), and use internal credit with the same rights and under the same conditions as local companies with national capital (art. 7 FIL). Pursuant to art. 2 FIL, foreign investor means any natural or legal person domiciled outside the national territory, holder of a foreign capital investment[3], and local foreign capital companies[4], when they are investors in other local companies (art 2, FIL)

[3] Foreign capital investment means a) any capital contribution belonging to foreign investors applied to economic activities carried out in the country; b) the acquisition of shares in the capital of an existing local company, by foreign investors.

[4] Local company with foreign capital means any company domiciled in the territory of the Republic, in which natural or legal persons domiciled outside it, are directly or indirectly owners of more than 49% of the capital or have directly or indirectly the amount of votes necessary to prevail in shareholders 'meetings or partners' meetings. Conversely, local company with national capital means any company domiciled in the territory of the Republic, in which natural or legal persons also domiciled therein, are directly or indirectly owners of not less than 51% of the capital and have direct or indirect ownership of the number of votes necessary to prevail in shareholders 'meetings or partners' meetings.

In general, foreign investors who want to invest in Argentina, either by starting up new businesses or acquiring existing businesses or companies, do not require prior government approval except in regulated industries or for general rules such as antitrust regulations.

Foreign investment may be made in free convertible foreign currency, capital goods, profits or capital in national currency belonging to foreign investors (provided they are legally able to be transferred abroad), capitalization of external credits in freely convertible foreign currency, intangible assets and other forms of contribution that are contemplated in special regimes (art. 3, FIL).

Besides the general framework whose provisions are laid down in the FIL, it is important to note that Argentina has signed various foreign investment guarantee treaties. Some of them insure investments against political risks, such as the availability and the right to transfer foreign currency, expropriations or similar measures, breach of contract by the government of the host country, war and civil disturbances, among other risks. In most cases, prior approval of the legality of the investment and insurance coverage by the government of the host country is necessary[5]. In general terms, in said treaties, Argentina undertook to give fair and equitable treatment to investors originating from the signatory countries and submitted to the jurisdiction of international arbitral tribunals for the settlement of disputes.

4. Conclusion

China has been showing to the world its brand-new development and economic vitality through Chinese 40-year “Reform and Opening-up” and “One Belt, One Road Initiative”. When continuously making the process of opening-up further and deeper, China simultaneously releases remarkable economic dividends to the different industries and fields around the world. In the meantime, in order to make a better balance between potential profits and the cost of compliance, foreign investors are suggested to pay attention to the “red line” of security review system.

Similarly, throughout the years Argentina has shown to the global community that it welcomes foreign direct investments. In this regard, it is worth noting that Argentina’s foreign investment regulations foresee no security reviews (unless specified otherwise in ad-hoc regulations) and also the country has signed numerous international treaties aimed to immunise foreign investments from political or legal risks and thus provide additional safeguards to foreign investors.

[5] Since 1990, and with the purpose of increasing foreign investment in the country, Argentina has signed treaties to promote and protect foreign investment with numerous countries, including the United States, Italy, Belgium, United Kingdom, Germany, Switzerland, France, Poland, Chile, Spain, Canada, Turkey, Egypt, the Netherlands, China, Denmark, Hungary, Finland, Korea, Portugal, Israel, Australia, Peru, Venezuela, Bolivia, Mexico, Russia, South Africa, India, New Zealand and Japan.

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