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Much ado about nothing?

State-controlled entities and the change in German investment law

by

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The rise of sovereign wealth funds (SWFs) and state-owned enterprises (SOEs) -- together state-controlled entities (SCEs) -- has led to concerns that SCEs could threaten national security by following political rather than mere commercial goals with respect to their foreign direct investment (FDI). While developed countries acknowledged that the rise of SCEs should not lead to new barriers to FDI, several have changed their legislation to expand government oversight of FDI flows. In 2009, Germany also tightened its foreign investment regime. What are the first experiences with this change in German investment law?

In April 2009, an amendment to the German Foreign Trade and Payments Act entered into force. According to the new law, the Federal Ministry of Economics and Technology (BMWi) can review foreign investments and can suspend or prohibit transactions that threaten to impair national security or public order. The new law applies to an acquisition of voting rights of 25% or more of a listed or non-listed German company by non-EU or non-European Free Trade Association purchasers; it does not explicitly discriminate between private or public foreign investors.¹ The law was prepared mainly before the financial crisis and was patterned, at the end, on US legislation.

According to current legislation, it is not mandatory for foreign investors to submit notifications of the acquisition of a German firm. Rather, the BMWi collects information about M&As by foreign investors and may review these transactions within three months. In 2008, the BMWi

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¹ Thomas Jost, "Sovereign wealth funds and the German policy reaction," in Karl P. Sauvant, Lisa Sachs and Wouter P.F. Jongbloed, eds., *Sovereign Investment: Concerns and Policy Reactions* (New York: OUP, forthcoming 2012).

expected that only about ten foreign investments per year would be reviewed. Foreign investors who are not sure whether their investments raise national security concerns can request a certificate of non-objection. Many economists and political commentators criticized the change of the German investment law, whereas the Government argued that the new law is only pre-emptive and will not be used to discriminate against SCEs.

So far, the German authorities have applied the new law carefully. From April 2009 to December 2011, no foreign acquisition of a German company was suspended or prohibited, and no review process was initiated by the BMWI. There were 99 cases during that period in which foreign companies applied for certificates of non-objection. In 98 cases, the foreign investors received the certificate, on average, within two weeks. In one case, the potential foreign investor refrained from its investment for unknown reasons.²

In recent years, investments by SCEs in the German corporate sector have risen noticeably. Their FDI is not shown separately in the German inward FDI stock statistics; but FDI from economies that host SCEs (e.g. China, Iran, Russia, United Arab Emirates) has risen strongly in the past decade -- from less than US\$ 2 billion in 2000 to US\$ 8.5 billion in 2009.³ SWFs have acquired stakes in several well-known German companies. For example, at the end of 2009, Qatar Investment Authority acquired a large stake in Volkswagen AG for US\$ 9.6 billion, raising its share in the world's third largest car producer to 17%. Most of these investments were under the 25% threshold that could provoke a review in case of security concerns. However, SCEs from countries of the Gulf Cooperation Council have also acquired several smaller sized German companies that are not listed on stock exchanges. In most of these cases they acquired more than 50% (and often 100%) of the equity capital of the German company.

Despite the change of its legislation, Germany has remained open for FDI. In 2010, the OECD continued to rank Germany among the most open countries for inward FDI worldwide, far ahead of France, Japan, the United Kingdom, and the United States. In the United States, for comparison, the Committee on Foreign Investment reviewed 313 transactions within a period of three years (2008-2010), of which 30% resulted in investigations.⁴

The careful handling of the new law and the increase of SCEs' investments in Germany can be interpreted in different ways: on the one hand, the change of the investment law was successful and passed a practical test as Germany remained an open business location. On the other hand, one could ask whether the German authorities had overreacted in changing the law by doing much about nothing. Like in most other economies, the public debate on restrictive measures against SCEs' investments has calmed down in Germany. In 2011, there were no reported changes of national investment laws with respect to national security in developed countries. Since the Lisbon Treaty took effect, the EU has gained the competence concerning FDI. Practical implications for Germany's legislation are still uncertain.

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² Information provided by BMWI. An official published report of the Ministry is not available.

³ Thomas Jost, "Inward FDI in Germany and its policy context, update 2011," *Columbia FDI Profiles*, November 19, 2011.

⁴ Committee on Foreign Investment in the United States, *Annual Report to Congress*, December 2011.

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