KEY POINTS

- Investments in the UK defence sector are less regulated than in France and Germany.
- French regulations are strict requiring prior authorisation and licences.
- In Germany, the far-reaching powers of intervention as regards both acquisitions by foreign investors and the requirement for licences, means that contractual change-of-control clauses are not necessary.

Feature

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The legal framework for foreign investment in the French, UK and German defence sector

This article provides a comparative overview of the legal framework for foreign investment in the defence sector in France, the UK and Germany, highlighting the differing approaches of the state.

Due to several factors, in particular relating to the reduction of defence budgets and high competition between national defence groups, the defence sector is becoming more consolidated in Europe. There are some forerunners. In 2012, there was the merger attempt between BAE Systems and EADS/Airbus group. More recently, in France, the French group Nexter Systems was privatised in view of its partnership with the German group Krauss-Maffei Wegmann (KMW) to create a leading European player in the land defence sector. Also, BAE Systems and Dassault Aviation entered into a partnership with the UK and French governments to create a new generation of unmanned jet.

Beyond political stakes, such mergers and strategic alliances present legal challenges, for example: (i) foreign investments control; (ii) obtaining certain permits or licences to conduct defence activities, which may face change of control issues; and (iii) restrictions and obligations around government contracts.

This article aims to provide an overview of the legal framework of investments in the defence sector in France, the UK and Germany.

French law is, unsurprisingly, quite strict. The control implemented by public authorities is carried out at several levels. Thus, some acquisitions, even of a minority interest, may require the prior approval of the French Ministry of the Economy. Furthermore, public authorities are also likely to withdraw certain permits or licences required to conduct defence activities in the event of a change of control of defence groups. Lastly, public procurement contracts regulations enable public co-contractors to terminate contracts early for any reason in the "public interest", which could include a change of control of the private co-contractor.

On the contrary, investments in the UK defence sector are less regulated than in France. Moreover, regulation does not derive from statutory provisions. Non-statutory restrictions are presented below.

Finally, the legal framework of foreign investments in the German defence sector is akin to the French one: investments are subject to strict official control. The trigger for adoption of this legislation was the takeover of the Howaldtswerke Deutsche Werft AG group (HDW – construction of conventional submarines) by US financial investor One Equity Partners in 2002 – a transaction that the German government was unable to exert any influence on at the time.

LEGAL FRAMEWORK OF FOREIGN INVESTMENTS IN THE FRENCH DEFENCE SECTOR: THE PROTECTION OF NATIONAL DEFENCE INTERESTS

In order to be subject to the prior approval of the French Ministry of the Economy, investments must qualify as "foreign investment" and relate to a "sensitive" activity, according to the criteria defined by the French Monetary and Financial Code (CMF).

More specifically, the prior authorisation regime depends on the origin of the investor (EU[1] or non-EU), as this determines both: (i) the scope of the operations considered as "foreign investments"; and (ii) the list of "sensitive activities". The regulations are more restrictive for a non-EU investor.

In what situations can a foreign investment consisting in the acquisition of a minority shareholding in a defence group be subject to prior approval?

There are at least three situations pursuant to the regulations relating to foreign investments provided by the French Monetary and Financial Code (FMFC). First, where the acquisition by a non-EU investor consists of a 33.33% (or more) shareholding or voting rights in a company that has its registered office in France.[2]

Second, where the acquisition of a minority shareholding grants the foreign investor (whether EU or non-EU) "joint-control" over the target company. A minority shareholder will be considered to jointly control another company when it holds veto rights on the strategic decisions of the company, (eg the appointment of the management). On the contrary, if the governance rights essentially aim at protecting the value of its investment, the foreign investor will not be considered as jointly-controlling the target company.

Third, prior approval may be required where a foreign investor (whether EU or non-EU) acquires a minority interest in a partnership with no share capital governed by French law.

The French administration considered under the previous regulations on foreign investments that the acquisition of a minority interest in an Economic Interest