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Introduction
Andrew W. Shoyer, Sven De Knop,
Jen Fernandez and Todd Friedbacher
Sidley Austin LLP

INTRODUCTION

Contributed by: Andrew W. Shoyer, Sven De Knop, Jen Fernandez and Todd Friedbacher, **Sidley Austin LLP**

Sidley Austin LLP acts as a one-stop shop for global issues and disputes, and its international trade practice works across offices in Brussels, Geneva and Washington, DC. With more than 60 practitioners, the group advises on customs, export controls and sanctions, investment screening/CFIUS, negotiations, trade defence and WTO disputes. Members of Sidley's international trade practice have served in numerous US government and international organisation roles involving the regulation of imports and exports. The firm's clients benefit from its experienced trade lawyers, PhD trade economists, specialised senior trade advisers and a specialised trade accountant. In addition to its WTO practice, Sidley advises companies and governments on high-level trade policy issues before Geneva-based international organisations such as the WHO and the WIPO. The firm has an unmatched track record of litigating in customs, regulatory and trade defence cases before the Court of Justice of the European Union and the General Court of the European Union.

Contributing Editor

Andrew W. Shoyer co-leads the global arbitration, trade and advocacy practice at Sidley Austin LLP, and focuses on the implementation and enforcement of international trade and investment agreements. He also advises on compliance with OFAC economic sanctions and BIS export controls. Andy spent seven years at USTR, serving most recently as legal adviser in the US Mission to the WTO in Geneva. He was the principal negotiator for the USA of the rules implementing the WTO Dispute Settlement Understanding, and has briefed and argued numerous WTO cases before dispute settlement panels and the WTO Appellate Body.

Co-authors

Sven De Knop is an advocate in Sidley Austin's global arbitration, trade and advocacy group, and focuses his practice on international trade law and EU law and regulations. He assists clients in international investigations and enforcement actions, including in the areas of trade defence (including anti-subsidy investigations), economic sanctions and export controls, and customs. Sven also assists clients in understanding how the relevant legal framework applies to their business and in the design and implementation of compliance programmes, and with internal investigations and compliance audits. A significant part of his practice concerns transactional support, where he assists in identifying and mitigating investment, foreign subsidy and trade controls risks.

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Jen Fernandez is a member of Sidley Austin's global arbitration, trade and advocacy group. She focuses her practice on international trade compliance, specifically export controls and economic sanctions, and US foreign investment reviews before the Committee on Foreign Investment in the United States (CFIUS). She advises clients on export controls and sanctions risk assessments and national security risks, including in connection with investments, offerings and acquisitions. Jen also conducts internal investigations, handles voluntary self-disclosures, and designs and implements trade controls compliance programmes.

Todd Friedbacher co-founded Sidley Austin's Geneva office in 2002, and serves both as the managing partner of the office and as a member of the firm's executive committee. By leveraging the powerful market access and enforcement tools provided by the WTO treaty and the hundreds of other bilateral and regional trade agreements in place worldwide, he has helped clients address critical trade and regulatory barriers impacting their ability to move, sell and protect goods, services and intellectual property across borders. A recognised leader in international trade and WTO law, Todd has represented clients in more than 55 WTO disputes, involving more than 90 distinct WTO dispute settlement proceedings, in his 25 years of practice.

Sidley Austin LLP

1501 K Street NW
Washington, DC
20005
USA

Tel: +1 202 736 8326
Fax: +1 202 736 8711
Email: ashoyer@sidley.com
Web: www.sidley.com

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Continuing Trade Tensions Create Increasing Challenges

The legal landscape for cross-border trade and investment has been dominated by the war in and around Ukraine, and efforts by the United States and the EU to restrict China's access to sophisticated supercomputing and semiconductor technology. The EU, for its part, is actively pursuing regulation to protect its industry and level the playing field caused by differences in the level of regulation in areas such as climate action, labour and human rights, and subsidies. These trends are likely to continue through 2024.

Business leaders charged with developing strategies for the future will need to adapt to the following:

- the new reality of increased sanctions, export controls and tariffs;
- more regionalised and complex supply chains, impacted by increasingly stringent due diligence and reporting requirements related to responsible sourcing (including in relation to, eg, forced labour, greenhouse gas emissions, critical raw materials, etc);
- increased trade remedy protections; and
- enhanced scrutiny on (foreign) investments and trade, likely subject to complex foreign investment screenings and foreign subsidies investigations.

However, while risks abound, so do opportunities.

Not long ago, tariffs remained something of an afterthought for most products imported into the USA – but, in 2018, the country doubled its tariff revenue. Furthermore, in 2020, the UK left the EU, sparking discussions on the tariff treatment for goods moving between the EU and the UK. Many predicted that the Biden administration would reduce tariff levels aimed at China, but that has not occurred. And the impact of high tariffs is felt keenly in Europe, where they may contribute to overall inflationary pressures felt across the globe.

Although the spike in US tariffs emanated in large part from trade tensions with China, they led to tariff duels with the likes of Turkey, India and the EU. The result was an increase in prices for goods such as aluminium, steel and washing machines.

The response to Russia's further invasion of Ukraine in February 2022 has combined asset freezes, import and export restrictions extending to key services sectors (most notably banking) and new investment bans. In taking action aimed at Russia, the EU, UK and USA have moved aggressively and in relative concert.

In contrast, the USA has imposed unilaterally significant export controls on China, covering supercomputing technology and semiconductor manufacturing, with the Netherlands and Japan having followed suit.

There has also been a stronger focus in trade restrictions on human rights and sustainable sourcing, adding an additional layer of complexity to compliance. The EU so-called carbon border adjustment mechanism started applying, which aims to impose reporting obligations and a carbon charge on imports of certain products for emissions released during their production.

China has made limited use of its export control regulations and the regulatory structure for an "Unreliable Entity List", adopted to counter the US Entity List.

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The importance of technology has also brought tech companies – even early-stage start-ups – into the fray.

Here are five things that business leaders and their international trade counsel must consider in navigating the regulatory challenges ahead.

Understand your supply chain – and look for patterns

There are hundreds of international trade agreements – bilateral, regional – that remain in force and serve as a bulwark against protectionist forces. Multinational leaders have to analyse that web of agreements and take advantage of reliable supply chain relationships.

Leverage government allies

Executives and board members at large corporations should activate their network of natural government partners to ensure that a diversified supply chain does not fall apart in other parts of the world.

Sourcing decisions are not just about efficiency – politics is a key factor

In the past, business leaders and legal counsel spoke of rationalising supply chains. Executives would look at an overlay of different trade agreements and decide, for example, that it would make sense to do a degree of manufacturing in Colombia, take the finished product to Peru, and then assemble it in Mexico. The decisions were based almost entirely on efficiency. Going forward, these decisions should factor in the politics of trade and supply chain regulation, and the risk of implicating subsidy-related investigations.

Diligence and rationalising third-party reliance

Third parties can pose risks, especially if business leaders are not aware of, for example, the source of foreign manufacturers' materials or the markets that channel partners are serving. From an enforcement perspective, authorities expect operators to take responsibility and exert more control over their supply chain.

Think about exports in co-ordination with imports

Companies need to think holistically about international trade compliance, which means considering imports and exports in tandem, and not just in terms of goods flows but also in terms of services and investment flows. For instance, the USA has put a number of restrictions on technology transfers to certain Chinese companies. Thus, even if tariffs may not pose a danger, a global company will need to consider relationships with manufacturers with respect to these technology transfers.

The recent slide towards economic nationalism is not historically unique; governments have long responded to economic downturns with policies intended to bolster domestic industry, often at the expense of competitors abroad. Trade agreements limit the discriminatory action that governments can take at moments they are most inclined to do so.

COVID-19 and the consequent recession prompted governments worldwide to offer subsidies aimed at bolstering domestic businesses. Just as in previous recessions, experienced observers agree that the new polices will trigger a slew of anti-dumping and anti-subsidy litigation – at the WTO and elsewhere – claiming the subsidies had a discriminatory or otherwise unfair impact on foreign competitors.

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Governments are generally permitted to give below-market funding to domestic players in a given industry, as long as they stay within certain bounds. If subsidies go on to cause aggravated economic harm to foreign competitors in global markets, it can be cause for litigation and, in the EU under the anticipated Foreign Subsidies Regulation, impact the ability to engage in M&A transactions or participate in public tenders.

Foreign Investment: Impediments Here to Stay

During 2020, long-awaited regulations came into force that greatly expanded the reach and authority of the Committee on Foreign Investment in the United States (CFIUS). At the same time, the EU foreign investment screening framework entered into full application. Despite being subject to each member state's interpretation, this framework reflects a growing movement towards a more US-type approach to investment screening by governments around the world.

As with seemingly every other element of international trade, COVID-19 and related supply chain shortages accelerated and expanded that trend – and not just to the usual suspects.

Historically, investment screening was perceived to be necessary only for very sensitive sectors, if at all. However, the COVID-19 pandemic and related issues around the supply of PPE, vaccines and medicines – plus a more general concern about foreign investors raiding undervalued assets – created an urgency for screening foreign investment in much wider sectors of the economy.

Hence, several EU member states – including Germany, Italy and Spain – accelerated (repeated) reform to provide additional protections to, for instance, domestic healthcare industries. Now 25 of the 27 EU member states have comprehensive investment screening regimes in place or are in the process of adopting one. In 2023, FDI screening regimes entered into force, inter alia, in Belgium, Bulgaria, Estonia, Luxembourg, the Netherlands, and Sweden.

Other jurisdictions around the world similarly adopted new or more stringent investment screening legislation. For example, in January 2022, the UK started to apply a comprehensive investment screening regime, which has already led to a significant number of transactions being subject to screening. In 2023, Switzerland started the process of adopting FDI screening regimes. In the USA, some fear predatory investment in distressed assets, although CFIUS is likely to rely on the existing expansions of its jurisdiction and mandatory filing requirements to address these fears.

Investors into the USA, the EU and other jurisdictions, even when only making indirect investments, may have to file mandatory notifications where they did not before; sectors such as healthcare, pharmaceuticals and information technology now fall under that umbrella. The scope of investments covered has been significantly expanded.

This means that investors need to take a more strategic approach. Business leaders and their counsel need to consider at least the following factors:

- the nature of the buyer and/or the vulnerability of the asset;
- the investor's appetite for risk;
- the implications on deal timing and uncertainty; and
- the disclosures and potentially onerous procedures involved as part of the deal process.

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The prevalence of foreign investment screening among like-minded countries may also lead to increased collaboration, which could force companies to co-ordinate various filings for multi-jurisdictional investments. One of the newer aspects of CFIUS regulations offers certain exemptions to investors from select countries; while the UK and Canada are currently the only two countries on this list (and for a trial period only), others may very well be added further down the line.

In the EU, the EU Investment Screening Regulation (No 2019/452) has fully applied since October 2020. Notably, it requires co-ordination amongst member states and with the European Commission's Directorate-General for Trade. Experience shows that (at least some) member states are making extensive use of the co-ordination mechanism.

Moreover, the EU Investment Screening Regulation significantly contributed to the harmonisation of more expansive screening legislation across the EU. As a result, more transactions undergo investment screening in the EU. Investors should be ready to assess investment risks relating to investment screening upfront and adopt risk mitigation strategies to address potential issues concerning the impact of a planned investment in the EU member state(s) of investment and in other member states.

In particular, investors should take care when entering into negotiations and arrangements with targets, especially regarding information-sharing in the context of due diligence and the implications of investment screening on the transaction timeline. In that regard, it is important to take investment screening into account when structuring transactions and when drafting transactional documents, including by considering the appropriateness of:

- a sign and close mechanism;
- ensuring that all parties co-operate to ensure that regulatory approval is obtained; and
- allocations of rights and obligations pending approval.

As with the other issues and challenges buzzing around international trade right now, heightened investment screenings present both a slide towards protectionism and opportunities for enhanced co-operation.

In addition, whereas investment screening regimes, so far, have focused on inward investments, there has been a recent focus on outward investments and possible national security aspects of transferring certain technologies and know-how abroad. Rules on outward investments have already been adopted in the United States, and the EU is expected to follow shortly.

On 12 July 2023, the EU's Foreign Subsidies Regulation started applying. This Regulation aims to address the potentially distortive effects on the EU market of subsidies from non-EU countries. It provides for three tools to review foreign subsidies – namely, pre-closing notification and review tools for certain M&A deals and EU public procurement procedures, and a general tool that will allow the European Commission to investigate individual companies or sectors. The notification requirements for M&A deals and procurement procedures started applying on 12 October 2023. The M&A notification requirements are separate from existing FDI and merger control regimes, hence adding a layer of complexity in deal making. Companies active in the EU should take pre-emptive steps to assess, mitigate and manage the regulatory risks arising from the regulation.

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