SIMMONS' COMPETITION/ANTITRUST PRACTICE

Foreign Direct Investment Regimes in Europe

The United Kingdom

Updated as of July 2023

The United Kingdom

Summary

- On 29 April 2021, the National Security and Investment Act (NSI Act) was given Royal Assent and came into into force on 4 January 2021.
- The new regime did not replace the public interest elements of the merger control regime but has replaced the national security consideration.
- The new regime has retroactive effect.
- The new regime focuses on acquisitions of 25% or more of a target company which is engaged in a sensitive sector of the UK economy. Such an acquisition must be notified to and approved by the UK Government before completing.
- Even if an acquisition falls outside the mandatory regime above, the UK Government may still decide to call in the transaction for review and if deemed to pose a "national security risk", it can be blocked. To address this inherent risk, parties may voluntarily notify the UK Government of a transaction.
- The regime applies not only to fresh investments/acquisitions, but equally to the increase of existing stakes. It may therefore also be triggered by follow-on investments, as well as by a reorganisation or share buyback which results in a party's shareholding increasing.

The United Kingdom

Contents

The United Kingdom

FDI Regime: NSI Act

National Security and Investment Act (NSI Act)

- The National Security and Investment Act (NSI Act) (see here) came into force on 4 January 2021.
- The NSI Act provides the UK Government with stand-alone powers to screen investments to intervene in any transaction giving rise to a risk to national security.
- The regime does not replace the public interest elements of the merger control regime but has replaced the national security consideration.
- This regime has retroactive effect, i.e. the regime covers any qualifying investment completed on or after 12 November 2020.

Key aspects of the new regime

- The regime focuses on acquisitions of 25% or more of a target company engaged in a sensitive sector of the UK economy.
- Such an acquisition must be notified to and approved by the UK Government before completing.
- Even if an acquisition falls outside this mandatory regime, the UK Government may still decide to call in the transaction for review (up to 5 years after the transaction).

The United Kingdom

FDI Regime: NSI Act

Investments likely to attract scrutiny

- There are three main ways in which "national security risk" will be analysed:

  1. Target risk: the target is active in one of the sectors identified by the UK Government as an area where more national security risks are likely to arise (mandatory notification sectors – see here).

  2. Control risk: the type and level of control or influence being acquired over an entity or assets.

     - A person acquires control of a qualifying entity (inc. companies, LPs, partnerships, trusts) or a qualifying asset (inc. tangible assets, e.g. real estate, and intangible assets, e.g. IP)

     - 'Control' tied to breaching various voting rights / shareholding thresholds (25%, 50%, 75%), the ability to secure or prevent certain company resolutions, or material influence (may be deemed to exist in relation to a low shareholding, potentially even below 15%).

  3. Acquirer risk: details of the parties which the Government considers more likely to pose a national security risk due to their status (e.g. affiliations with hostile states / organisations).

- The regime applies not only to fresh investments/acquisitions, but equally to the increase of existing stakes (25%, 50%, 75%). It may therefore also be triggered by follow-on investments, as well as by a reorganisation or share buyback which results in a party's shareholding increasing.

The United Kingdom
FDI Regime: NSI Act

Buyer's nationality

- There is no distinction based on the buyer's nationality – the regime applies equally to all investors, both foreign and domestic.
- Note however that the Secretary of State has powers to exempt certain acquisitions from the mandatory notification regime on the basis of the characteristics of the acquirer.

UK nexus

- The jurisdictional test requires that the entity or asset an investor is acquiring is from, in, or has a connection to the UK.
- As such, entities and assets may be "qualifying entities" and "qualifying assets" if they are outside or not from the UK but have a connection to the UK.
- An entity being acquired is likely to be classed as a "qualifying entity" if it (1) supplies goods or services in the UK; (2) carries out research and development in the UK; (3) has an office in the UK from which it carries on activities; (4) oversees the activities of a subsidiary that carries on activities in the UK; (5) supplies goods to a UK hub which sends the goods onto other countries.

The United Kingdom

FDI Regime: NSI Act

Possible outcomes and consequences of "gun-jumping"

- The possible outcomes are (1) approval, (2) approval with conditions (e.g. restrict size of stake, ring-fence sensitive info/tech, commitment to maintain UK HQ or presence, maintain security of supply chain), (3) outright prohibition if unacceptable risk to national security.
- For notifiable transactions, (1) the transaction is automatically void, (2) penalties of up to 5% of global turnover or £10m (whichever is the higher) apply, (3) possible imprisonment for up to 5 years.
- All other transactions remain subject to the Secretary's call-in power for up to 5 years after the transaction (or up to 6 months from the date the Secretary becomes aware of the transaction).
- Note: Retroactive effect – any transactions completed on or after 12 November 2020 fall within the regime.

The United Kingdom

FDI Regime: NSI Act

Mandatory notification sectors

- The regime targets 17 key sectors (see below) including communications, defence, energy and transport. The UK Government has published further details about the key sectors (available here).
- However, the regime is not limited to the key sectors – other qualifying transactions which raise a national security risk may also be caught.

1. Advanced materials
2. Advanced robotics
3. Artificial intelligence
4. Civil nuclear
5. Communications
6. Computing hardware
7. Critical Government suppliers
8. Critical emergency services suppliers
9. Cryptographic authentication
10. Data infrastructure
11. Defence
12. Energy
13. Military and dual use
14. Quantum technologies
15. Satellite & space tech
16. Synthetic biology
17. Transport

The United Kingdom

FDI Regime: NSI Act

Procedure

Is the regime **mandatory** (i.e. are parties obliged to notify of the transaction)?	This is a hybrid investment review regime: 1) **Mandatory notification** and clearance regime for specific sectors for acquisitions of 25% or more of a target company 2) **Voluntary notification** and call-in regime across all sectors and any transaction posing a risk to national security
Is the regime **suspensory** (i.e. must parties wait for an approval decision before completing a transaction)?	• Mandatory notification: transactions must first be **cleared** before parties can complete the transaction • Voluntary notification: parties can complete the transaction **without** obtaining clearance but it remains subject to the Secretary's **call-in** power for up to 5 years after the transaction (and up to 6 months from the date the Secretary becomes aware of the transaction)
What is the **timing** between an approval decision being issued and the commencement of a review by the authority?	• Following mandatory / voluntary notification: **30 business days** from acceptance of a notification to decide whether to issue a call-in notice for the transaction • If call-in notice issued: **additional 30 business days** to decide whether to clear, impose remedies on, or block transaction – extendable by **additional 45 business days** or longer, if agreed by acquirer • Clock **stops** while information requests pending

The United Kingdom
FDI Regime: NSI Act

Investment Security Unit (ISU)

- The Government has established a new unit, originally in BEIS, now within the Cabinet Office, the Investment Security Unit (ISU), which will receive and manage notifications under the NSI Act.
- The ISU is already operational and available to respond to queries on preliminary basis (not binding).

Next steps

- The Government has drafted and adopted secondary legislation and guidance on the application of the new regime (including call-in notices and the notification system).
- The Government has issued a policy statement on how the call-in power will be used.
- The Government has issued guidance on the definitions of the 17 sectors.

The United Kingdom

FDI Merger Control Regime: Transactions subject to review

Public interest intervention

- The UK Government can intervene in certain "relevant merger situations" (see page 11), either on its own initiative or on the recommendation of the CMA, by issuing a public interest intervention notice ("PIIN"), as provided for in the Enterprise Act 2002 ("EA").
- This acts as a screening mechanism for acquisitions of UK businesses, and can block transactions in certain situations, on grounds of "public interest".

The United Kingdom

FDI Merger Control Regime: Transactions subject to review

What types of transactions are subject to review?

The Secretary of State can intervene in relation to:

Public Interest Mergers

- The Secretary of State can issue a public interest intervention order ("PIIN") in relation to a relevant merger situation, for reasons of: (1) national security, (2) plurality of the newspapers and the media, (3) stability of the UK financial system, and (4) public health emergencies.
- The Secretary of State has powers to amend the provisions in the EA, by adding or removing considerations by way of an Order, where appropriate. When the EA was first enacted it only covered national security, whereas now additional considerations have been added, most recently regarding public health emergencies in light of the Covid-19 pandemic.

Special Interest Mergers

The Secretary of State can issue a special public interest intervention order ("SPIIN") in relation to special interest mergers even where the merger does not meet the usual threshold for intervention, providing that:

a) one of the merging parties is a governmental contractor involved in confidential defence and a public interest issue arises, or

b) one of the parties supplies at least 25% of all newspapers or broadcasting.

Certain critical technology mergers

- Transactions may otherwise be covered by the lower turnover and share of supply thresholds applicable to certain enterprises under section 23A of the EA.
- These lower thresholds relate to entities that are active in (1) military use goods or dual use technology; (2) multi-purpose computing hardware; (3) quantum technology; (4) advanced materials; (5) cryptographic authentication products; and (6) artificial intelligence.
- The more relaxed thresholds effectively provides for a lower barrier to additional scrutiny on certain transactions which are viewed as imperative from a national security or critical national infrastructure perspective.

The United Kingdom

FDI Merger Control Regime: Transactions subject to review

Can minority stakes be caught?

- Minority stakes can be caught, as the Secretary of State can intervene wherever there is a "relevant merger situation", which may include minority acquisitions.
- One of the criteria for such intervention is that "two or more enterprises cease to be distinct", i.e. where they are brought under common ownership or common control. Control exists where the enterprise is able to exercise material influence over the other enterprise (such as the ability to influence policy e.g. through voting rights as a shareholder).
- Under this relatively wide definition, a shareholding of 25% (the ability to block special resolutions) is likely to provide "material influence", and anywhere between 15% - 25% is likely to gain scrutiny.

The United Kingdom

FDI Merger Control Regime: Thresholds

The UK regime applies where certain threshold tests are satisfied; however the thresholds differ depending on the type of legal grounds on which the Secretary of State is intervening on.

Public Interest Mergers

The regime only applies if either the turnover test or "share of supply" test is satisfied.

- The turnover test requires the value of the UK turnover of the target company to be over £70 million.
- The "share of supply" test requires that, as a result of the merger, the combined enterprise will supply or acquire 25% or more of any goods or services in the UK, or a substantial part of the UK, or an existing share of supply of 25% or more is increased.

Special Interest Mergers

The usual "share of supply" and turnover tests are not required, provided that:

(a) one of the merging parties is a governmental contractor involved in confidential defence and a public interest issue arises, or

(b) one of the parties supplies at least 25% of all newspapers or broadcasting.

Certain critical technology mergers

In cases regarding specific industries and activities (military use goods or dual use technology; multi-purpose computing hardware; quantum technology; advanced materials; cryptographic authentication products; and artificial intelligence), the usual tests are amended:

1. the requirement for there to be an increase in the share of supply is removed in instances where the share is already 25% or more; and
2. the turnover test threshold is reduced from £70 million to £1 million.

The United Kingdom

FDI Merger Control Regime: Procedure

Is the regime **mandatory** (i.e. are parties obliged to notify of the transaction)?	Notification to the CMA of a transaction is **not mandatory**, although the CMA has extensive powers to intervene after completion of a transaction.
Is the regime **suspensory** (i.e. must parties wait for an approval decision before completing a transaction)?	Firms can complete a merger **without** obtaining UK merger approval. However, if the CMA decides to investigate the merger despite a lack of notification, then the CMA has **wide powers** to impose interim measures, which can require the parties to hold the merging businesses separate and potentially unwind any already existing integration.
What is the **timing** between an approval decision being issued and the commencement of a review by the authority?	• The CMA has **40 working days** to complete the initial stage of its merger review process (its Phase 1 review). At the end of the Phase 1 review the CMA states whether it believes the merger results in a realistic prospect of a substantial lessening of competition, and if it does, it will launch an in-depth Phase 2 review. • The Phase 2 review is generally limited to **24 weeks**, and therefore resulting a total of just under 30 weeks from commencement of review by the authority before approval in a full Phase 2 referral case. • Where the Secretary of State refers a public interest or special public interest merger to the CMA, the CMA must generally deliver its report to the Secretary of State **within 24 weeks**. Within 30 days of receipt of the CMA's report, the Secretary of State shall make a decision in relation to the public interest or special public interest merger.

The United Kingdom

FDI Merger Control Regime: Procedure

How long does the authority have to commence a review before it loses jurisdiction to do so?

- The CMA has a 40 working day deadline to make a Phase 2 reference for completed mergers, which commences from the time that material facts of the case are made public, or the time the CMA is told of the facts (whichever is earlier).

What action can the authority take to protect national interests?

- The Secretary of State, once it has received the CMA's report setting out its recommendation as to whether it raises a public interest concern (following the Secretary of State's intervention notice), can refer the transaction back to the CMA for a Phase 2 investigation (see page 12 on timing). At this stage the CMA will prepare a detailed report regarding all competition concerns, including any specific public interest concerns. This is then returned to the Secretary of State for it to take the final decision as to whether the merger goes against the public interest.
- If this is found to be the case, the Secretary of State can take action to remedy and/or mitigate the effects of the merger, which can include blocking the deal if necessary. More commonly, however, the Secretary of State will ask the parties to provide undertakings to address the concerns, rather than resorting to blocking the deal.

The United Kingdom

Impact on M&A

- Greater levels of **due diligence** especially in relation to tech / critical infrastructure targets
- **Deal structure**: structuring around the regime is often unlikely to work – most regimes "look through" to indirect holdings
- **Protection against call-in**
  - Transactions could be subject to voluntary notification regime
  - Parties will need to think of the steps that can be taken now to safeguard against call-in (e.g. consider approaching BEIS)
- **Deal timeline**
  - What is the likelihood of approval or further review, and how does this impact the deal timeline? What should the longstop date be in light of this?
  - Will it be necessary to coordinate with other FDI / national security reviews across Europe?
- **Transaction documents**
  - Standard of efforts for obtaining approval
  - Specific efforts, e.g. do efforts include obligation to divest assets, or to resist litigation by the regulator etc.
  - Divestiture cap on amount of divestments or specified assets
  - Longstop date

The United Kingdom

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