WILLKIE FARR & GALLAGHER LLP

Foreign Investment Matters

UK National Security and Investment Reviews – Emerging Trends and Practice

February 24, 2023

AUTHORS

Philipp Girardet | Rahul Saha | Addiped Cheng

The UK's new investment screening regime under the National Security and Investment Act 2021 (*NSIA*) has been in operation for just over a year now. Upon its first anniversary, we set out below our key observations on how things have worked out so far.

The regime is managed on a day-to-day basis by the Investment Security Unit (*ISU*). The ISU was originally established within the UK Government's Department for Business, Energy and Industrial Strategy (*BEIS*) and overseen by the Secretary of State for BEIS, who was also the decision-maker under the regime.

Following the Government's decision earlier this month to restructure BEIS, the ISU now sits within the Cabinet Office. The head of the Cabinet Office, currently Oliver Dowdon, will replace the Secretary of State for BEIS as the decision-maker on whether to 'call in' a transaction and the outcome of any such review. The latest Government reshuffle means that the nascent regime has already lived through three leadership changes, including three Secretaries of State (Kwasi Kwarteng, Jacob Rees-Mogg and Grant Shapps) and now the head of the Cabinet Office (whose official title is the Chancellor of the Duchy of Lancaster), Oliver Dowdon.

The intervention rate under the NSIA is significantly higher than under its predecessor public interest regime

The Secretary of State intervened (ie imposed a final blocking order or conditions) in 14 deals in the first year under the NSIA. Of these, 5 deals were blocked and 9 were cleared subject to conditions to mitigate national security concerns. After a relatively slow start, there was a significant uptick in the ISU's activity towards the end of last year – 11 of the 14 interventions occurred in the four months from September to December 2022.

The rate of intervention under the NSIA represents a significant step change from the old 'public interest' regime under the Enterprise Act, which saw a total of only 24 reviews in the last 20 years. In its first three months of operation alone, the ISU reported that it screened over 200 notifications and called in 17 deals for an in-depth assessment. On an annualised basis, the ISU will have screened well over 800 notifications and called in at least 70 transactions for an in-depth review over its first year of operation.

The precise number of deals notified and called in for in-depth assessment will be confirmed in the ISU's next annual report, which is expected to be published in the summer.

Buyer nationality makes a difference to the likelihood and outcome of intervention, but other investors are not exempt from scrutiny

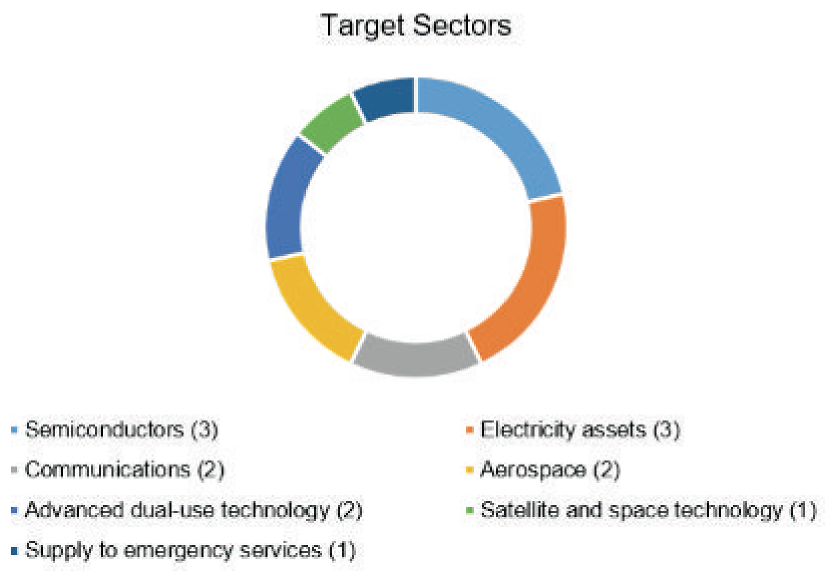
Unlike regimes in some other jurisdictions such as France and Germany, the NSIA applies not only to foreign investments, but also to domestic investments. That said, not surprisingly, buyers with ties to states perceived to be potentially 'hostile' to the UK have attracted a higher level of scrutiny.

Chinese or Chinese-backed buyers were involved in 8 of the 14 interventions to date. Of the 8 interventions relating to Chinese buyers, 4 deals were prohibited, and 4 were permitted to proceed on the condition that information barriers and other security measures be implemented to restrict the flow of information to the buyer and give the UK Government additional oversight of the target business. The only other transaction that was prohibited in 2022 involved a Russian-backed buyer.

However, buyers from 'friendly' nations are not immune to interventions as the Government has intervened in deals involving buyers from the US, Germany and the UAE. One intervention involved an investment by a domestic UK private equity buyer in a provider of secure communications solutions for the UK emergency services (Sepura).

The Government has intervened in a wide variety of sectors, with a focus on UK targets

The below chart illustrates the sectors the UK Government has intervened in to date.



As can be seen from this chart, the semiconductor and electricity sectors had the highest number of interventions. However, given the regime has been in operation for just over a year, it is too soon to draw any conclusions on whether the Government is focussed on specific sectors or if the above numbers are simply driven by the type of deals which happen to have been done over the last year.

Although the NSIA grants the UK Government jurisdiction to review the acquisition of foreign targets with only marginal UK nexus, the vast majority of the interventions to date have involved UK targets, with the remainder being targets with a UK business division. The ISU's practice to date is in contrast to the expansive jurisdictional approach taken by the UK Competition and Market Authority, which has not shied away from investigating and blocking transactions with tenuous nexus to the UK (eg Meta/Giphy and Sabre/Farelogix).

The table below summarises the buyer nationality, target sector and outcome of the 14 interventions in 2022.

Buyer nationality	Target sector	Transaction
Chinese	Semiconductors	HiLight Research/SiLight Semiconductor
		Newport Wafer Fab/Nexperia*
		Super Orange/Pulsic
	Vision sensing technology	University of Manchester/ Beijing Infinite Vision Technology Company
	Electricity asset	XRE Alpha/China Power
		Electricity North West/Red Rock Investment
		Stonehill project/Stonehill Energy Storage
	Aerospace	Ligeance Aerospace/Sichuan Development
US	Satellite	Viasat/Inmarsat
	Electron devices	CPI/Iceman
UK	Secure communications for emergency services	Sepura/Epiris
Russian	Broadband network	Upp Corporation/L1T FM
UAE	Aerospace	Reaction Engines/Tawazun
German	Mobile services	Truphone/TP Global Operations

Blocked
Cleared with conditions

**Nexperia has challenged the Government's decision in the High Court.*

Key Practice Points

Based on UK practitioners' experience of the NSIA regime to date, we would highlight the following practice points in relation to interactions with the ISU and the application of the NSIA:

- **Internal reorganisations require notification**: The legislative text of the NSIA indicated that internal reorganisations of businesses operating in specified sectors would require notification to the ISU. However, given the administrative burden this would impose, UK practitioners sought clarification. The ISU issued market guidance notes in July 2022 confirming that internal corporate reorganisations require mandatory notification where any 'qualifying entity' operates in a 'specified sector'. This means that where any new group entity acquires, directly or indirectly, a 25% interest in a qualifying entity, NSIA filings are required even where there is no change in ultimate control/ownership.

  The ISU's approach to internal reorganisations has generated a substantial increase in the number of mandatory filings and it is important to flag to parties at the outset that additional notification requirements may be triggered by any pre-closing and post-closing reorganisations.

- **The ISU proactively screens the market for deals that might be sensitive**: A Risk Assessment Unit within the ISU has recently started to screen the market for sensitive deals, and may send 'information notices' requesting information or an explanation for why a completed deal was not notified. The NSIA empowers the Government to impose criminal and civil sanctions for missed filings. It is understood that the Government has not imposed any sanctions to date.

- **The time the ISU takes to accept a filing varies**: According to the ISU's first Annual Report, the ISU took on average four to five working days from receipt of a filing to acceptance (ie starting the initial 30 working day review period). In our experience, the ISU has a good track record of accepting filings within a week. However, UK practitioners have noted some variability, with acceptances being delayed on occasion. In light of this, it is prudent to factor into deal timelines some leeway for a longer 'pre-acceptance' period where a NSI notification is required.

- **The reasons for 'call in' decisions are not always easily foreseeable based on public or management information**: Market reports suggest that deals with no obvious sensitivity or significant UK nexus may be called in for an in-depth assessment. Such uncertainty is inherent in any national security screening processes as even target’s management may not be fully aware of whether the target’s products have been used for sensitive purposes, eg by Government customers.

- **Interactions between parties and the ISU in the review period are very limited**: The nature of the review process is opaque. In-person interactions between parties and the ISU are infrequent and the ISU does not always specify its concerns during an in-depth review. While the sensitive nature of the assessment imposes certain restrictions on how transparent the ISU can be with parties, greater engagement with transacting parties would be helpful in allowing parties to assist the ISU with identifying potential deal conditions which could address the ISU’s concerns.

Further guidance to refine and clarify the application of the NSIA would be welcome

The ISU has only published 15 decisions to date, each typically no longer than a page and providing only very limited details concerning the ISU’s reasoning. The opacity of the review and decision-making process means that transacting parties that have submitted a filing on the basis of self-assessment are unable to gain meaningful insight into how the ISU has applied complex sector definitions in individual cases, and there is no body of precedent decisions to assist with self-assessments of whether a deal may trigger a mandatory filing.

Looking ahead, the ISU is expected to publish additional market guidance to refine and clarify the scope of application of the NSIA.

In the forthcoming second NSIA Annual Report, which will be the Government’s first full-year report covering the period from 1 April 2022 to 31 March 2023, the ISU will also publish further information and statistics on its operations to date.

Learn more about our Antitrust & Competition practice >

Read recent Willkie newsletters >