Land, loans and licences: a threat to the UK's national security?

July 2018

On 24 July 2018, the UK Government published proposals to review transactions on national security grounds. This briefing discusses key features of the proposals.

- **The proposals are directed at investments from potentially hostile foreign states.** The proposals note that some transactions could give rise to an increased risk of espionage, the disruption of critical national infrastructure and / or inappropriate leverage in geopolitical or commercial negotiations. The proposals suggest that these risks may arise in certain sectors in particular – national infrastructure, advanced technologies and services that are critical to the Government and emergency services. Underlining that this is a form of foreign investment control, the proposals indicate that foreign acquirers are more likely to pose a national security risk than UK-based or British acquirers. Reflecting the gravity of the harm the proposals aim to prevent, breaches of the rules would give rise to criminal as well as civil sanctions.

- **A much wider range of transactions are caught by the proposals than that under most merger control regimes.** For example, loans (e.g. where they are granted by potentially hostile lenders and / or on the basis of collateral over sensitive entities or assets), acquisitions of land (e.g. where that land is in close proximity to critical national infrastructure or government facilities) and acquisitions of intellectual property (e.g. where that IP is necessary for the supply of crucial services to national infrastructure) could all be reviewed under the proposed regime. Transaction due diligence will therefore need to take into account the broad scope of the proposed rules.

- **Reflecting the wide reach of the proposals, the Government expects 200 national security notifications to be made each year.** The Government considers that around 100 of these may be subject to a full assessment, with around 50 of these 100 requiring remedies. By comparison, in 2017 and 2018 (to date) there have been just five public interest reviews under existing powers, of which only two were on grounds of national security.

- **Notification under the proposed regime would be voluntary.** In contrast to the mandatory notification regime previously mooted, the Government would have powers to 'call in' transactions for review (potentially up to six months after the relevant trigger event has occurred) and parties could voluntarily notify their transactions. In principle, this gives a seller more flexibility to close a transaction quickly, if it can negotiate completion conditions that ensure that the buyer assumes the risk of a potential national security review post-closing. In reality, however, such flexibility is likely to be limited: larger transactions are in any event likely to be

subject to mandatory and suspensory merger filings in other jurisdictions and once a transaction is called-in completion will be prohibited until the review is complete.

- **A review under the proposed regime may be lengthy.** While the proposals emphasise a swift review process, experience of merger control and other regimes (such as CFIUS in the US) suggests that these reviews inevitably become front-loaded over time, in particular through pre-notification discussions with no binding deadline. Following voluntary notification, the Government could take up to 30 working days to decide whether to undertake a full national security assessment, with any subsequent full assessment then taking a further 30 working days (extendable by 45 working days and subject to powers to stop-the-clock if information requests are outstanding). The proposals therefore increase the likelihood of regulatory delay for transactions that could give rise to national security issues.

- **The proposed national security regime would be standalone and, where legal, would take priority over applicable merger control regimes.** In particular, the Government would have the power to clear an anti-competitive transaction where it had national security grounds for allowing the transaction to proceed. However, such powers would effectively only apply where the UK Competition and Markets Authority was the sole relevant merger control authority – the Government would be unable to over-ride the decision of other competition authorities (including the European Commission).

- **Except for transactions giving rise to national security interests, the pre-existing public interest regime would continue**. If and when these proposals come into force, then the national security provisions currently in force in the Enterprise Act 2002 (including those introduced by the Government as recently as June 2018) would fall away, with the pre-existing public interest regime continuing in place, currently only for transactions giving rise to media plurality and / or financial stability issues.

The Government has stressed that the proposals are a proportionate response to a real threat and in line with international developments (the proposals refer specifically to equivalent reforms in Germany, Japan and Australia, as well as the European Union's proposed foreign investment screening regulation). Nonetheless, they have the potential to introduce significant additional complexity for certain transactions. For those transactions, the proposals may have significant ramifications for timing and the outcome of parallel merger control review processes.

The consultation period ends on 16 October 2018.

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