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National Security & Investment Act 2021 One Year on – Key Lessons

The National Security and Investment Act 2021 ("**NSIA**") came into force on 4 January 2022, just over a year ago, introducing for the first time ever in the UK a standalone national security screening regime. The NSIA allows the UK Government, acting through the Department for Business, Energy & Industrial Strategy ("**BEIS**"), to scrutinise different types of transactions with a UK nexus and, if necessary, to impose conditions on, or even block, such deals if they could give rise to any relevant national security risk(s). To date, the NSIA appears to have been working effectively. This briefing discusses the top important trends emerging from the NSIA's first year in operation, exploring how the UK Government is exercising its powers under the new regime and the implications for investors and target businesses in practice.[1]

1 Most transactions are cleared swiftly and unconditionally – but not all…

The positive news is that, after a filing has been submitted, BEIS has been quick to confirm both receipt and that the notification is compete, taking on average two to three working days to do this. More positively still, once BEIS' review process commences it has generally cleared deals raising no national security concerns within 30 working days. However, parties should be aware that, in more complex cases, BEIS generally takes 24 working days to "call-in" deals for a more detailed review and the latter assessment can go on for over six to seven months. This is often because, during an in-depth assessment,[2] BEIS can issue information requests which "stop the clock" on the review timetable. Moreover, the in-depth assessment period is itself 30 working days in length and extendable by another 45 working days (and then, if deemed suitable, for a further undetermined period on top of that, but only by mutual agreement between BEIS and the relevant party(ies)). A further timing point to note is that BEIS will only accept notifications from parties to a relevant deal before signing provided there is a legitimate and realistic prospect that the deal will proceed (e.g., evidenced by the existence of heads of terms). However, should the structure of the deal change or not go ahead, BEIS must be notified immediately, which, in turn can also cause delays.

2 One of the most expansive national security screening regimes worldwide…

The NSIA can catch a broad array of different transactions and has proved to do so over the course of 2022. Share acquisitions are not only caught, but any asset deals (e.g., land, tangible (moveable) property, IP such as ideas, information, techniques or software) can also be caught. Indeed the relevant thresholds for both share and asset acquisitions can be very low, with BEIS able to claim jurisdiction in deals with share acquisitions potentially as low as c. 10% (based on the concept of "material influence"[3]) and in respect of deals involving the acquisition of the control over any relevant asset(s) to a "greater extent" than existed before the deal took place.[4] The NSIA also captures investments by UK acquirers (the acquirer does not have to be "foreign") and international transactions where the entity being acquired is neither based in the UK nor has any UK subsidiaries. Intragroup reorganisations, licensing activities, financial arrangements, employee incentive schemes and pensions, property arrangements and the appointment of liquidators/receivers can also trigger a filing requirement. The NSIA has also proven itself to be rather unpredictable at times. In 2022, we saw BEIS carry out an in-depth investigation and block a deal involving the acquisition of IP and contracts, an

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[1] For our other relevant NSIA briefings published in the last 12 months, please see also: (i) *A deep dive into the key aspects of the new NSIA regime*; (ii) *The long-awaited NSIA is now in full force*; and (iii) *The National Security and Investment Act 2021 – the impact on loans and finance transactions*.

[2] Please note that, in its initial 30 working day review period, whilst BEIS can issue information requests, this does not "stop the clock". Rather, it is only in respect of information notices issued during any in-depth assessment period that the review period can be paused. See BEIS' guidance document on the operation of the NSIA regime at: https://www.gov.uk/guidance/national-security-and-investment-act-guidance-on-acquisitions

[3] See the acquisition by *UAE's Tawazun Strategic Development Fund* of shares in *Reaction Engines* where material influence in a propeller and space technology company was proposed to be gained by a USE acquirer. The UK Government considered there to be a risk of dual use capabilities being covertly accessed by hostile parties and remedies were imposed.

[4] See *Beijing Infinite Vision Technology/University of Manchester* and *Stonehill Energy Storage/Stonehill Project Asset Development Rights.*

asset deal that did not even fall within the mandatory filing regime; only to reverse the order in part earlier in 2023.[5] This latter point, in particular, reinforces the broad scope of the NSIA regime and BEIS' fairly aggressive approach to enforcement.

3 More interventionist than expected…

BEIS has been a far more active and interventionist regulator than expected – in particular, compared to the old public interest regime under the Enterprise Act 2002, where the UK Government did not block a single transaction. Indeed, based on statistics as of 31 December 2022, BEIS has to date blocked five transactions[6] and imposed conditions on a further nine cases before a deal could close.[7] BEIS also has not been afraid to use its retrospective call-in power to investigate deals concluded before the NSIA came into force,[8] having used it in two of the blocked transactions.[9] There is also evidence that BEIS is increasingly contacting parties on deals that it considers should have been filed, albeit to date, no fines appear to have been imposed on parties for failure to file despite BEIS' power to impose heavy sanctions in this respect, including turnover-based fines, criminal sanctions and rendering the transaction null and void. Consequently, although the responsibility to submit a notification tends to fall on the acquirer (whether a mandatory or voluntary filing), acquirers have increasingly required targets (especially PE houses and their portfolio companies) to analyse the spectrum of their activities and set out in a report whether they consider any aspect of their businesses fall within any of the 17 sensitive key sectors (and other aspects of the NSIA). Targets should be prepared to provide extensive due diligence materials to satisfy investors, agree to

[5] See *Beijing Infinite Vision Technology/University of Manchester*. This case involved an initial order prohibiting the acquisition of intellectual property rights in vision-sensing technology by a Chinese company from The University of Manchester. However, this order was varied in January 2023, with BEIS allowing the University of Manchester to share the technology in certain circumstances (subject to the agreement of BEIS) and provided that the University of Manchester's obligations regarding its employees were clarified in each case. The fact that the final order was varied is interesting as it reflects the reality of balancing the protection of national interests against the fluidity of insight and technological exchange required for research and development to thrive.

[6] The prohibition decisions that have been made by BEIS to date concern: (i) *Beijing Infinite Vision Technology Co's* acquisition of intellectual property through a licence agreement with the *University of Manchester* relating to certain vision-sensing technology; (ii) Hong Kong-based *Super Orange HK Holding Limited's* acquisition of *Pulsic Ltd*, a producer of electronic automation products; (iii) the acquisition of *Newport Wafer Fab*, the UK's largest semiconductor plant by the Chinese-owned *Nexperia*; (iv) the Russian-backed investment company *LetterOne's* acquisition of regional broadband provider, *Upp Corporation*; and (v) *SiLight (Shanghai) Semiconductor Limited's* acquisition of *HiLight Research Limited*, a supplier of integrated circuits for optical communication.

[7] In *Epriis/Sepura,* which involved a UK acquirer, the parties were required to implement enhanced controls to protect sensitive information and technology from unauthorised access, as well as to provide rights of access to premises and information so that relevant agencies will be able to audit compliance with these security measures. In *Tawazun Strategic Development Fund/Reaction Engines Limited*, the substance of the remedies has not been published, but the Government's view was the that deal risked sensitive IP of Reaction Engines being covertly accessed by hostile actors, presenting a national security risk to the UK. In the acquisition of the *Stonehill project asset development rights* by *Stonehill Energy Storage Ltd*, the acquirer was required to obtain UK Government approval before appointing a power offtake operator and there was a restriction imposed vis-à-vis the sharing of information from the power offtake operator to the acquirer. In the acquisition of *XRE Alpha Limited* by *China Power International Holdings Limited,* the Government restricted both the management of power offtake and the provision of ancillary services required by National Grid to operators approved by the UK Government and restricted the sharing of information by the operator of the site with the acquirer outside of an inclusive list of permitted information. In *Viasat/Inmarsat*, the Government expressly issued a remedy to ensure the continued supply of strategic capabilities (relating to global mobile satellite communications) to the UK Government. In *Iceman/CPI* a remedy was imposed on a US acquirer to keep the R&D and manufacturing of atomic clocks (quantum technology) within the UK. (It is worth noting that atomic clocks are very precise and do not rely on satellites, which means that they offer both military and civilian benefits). In *Sichuan/Ligeance Aerospace*, the Government considered that the proposed acquisition by a Chinese controlled acquirer of a UK aerospace company required conditions which: (i) restricted information sharing; (ii) specified security measures; (iii) removed certain board representatives; (iv) required board appointment of a government observer; and (v) required notification of the transfer of certain assets. In *TP Global Operations Limited/Truphone Limited,* the Government required the acquirer to appoint a Chief Information Security Officer approved by the Secretary of State and to put in place telecoms information security measures on the acquirer, as well as requiring the acquirer to carry out a security audit by an UK Government-approved auditor to produce a report setting out any new security measures. As regards the acquisition of *Electricity North West Limited* by *Redrock Investment Limited*, although this deal was allowed to close subject to certain conditions, the investor ultimately decided that the restrictions were too onerous and did not proceed with the deal.

[8] Please note that BEIS has the retrospective power under the NSIA to call-in and investigate any deals which took place between 12 November 2020 and 4 January 2022. This time window represents the so-called interim period between the date the draft NSIA Bill was first presented to the UK Parliament and the date on which the NSIA regime ultimately came into effect after the underpinning legislation received Parliamentary approval and Royal Assent.

[9] See *Nexperia/Newport Fab* and *Upp Corporation Limited/LetterOne*.

condition precedent clauses to make completion conditional on all relevant approvals from BEIS and warrant their activities do not fall within the scope of the NSIA or trigger any mandatory notification.

4 Nationality agnostic or not…?

One of the most interesting aspects of the NSIA regime is that it is (at least nominally) agnostic towards the nationality (or country of incorporation) of any acquiring entity. This can be evidenced by the fact that UK-UK transactions can be (and often are) caught by these new screening rules. It is also evidenced by the fact that BEIS has, at least insofar as the need for an initial assessment is concerned, not distinguished between so-called "friendly" nations and others. BEIS has investigated deals involving nations such as the U.S., Australia and other European investors (e.g., Germany, France). Such factors distinguish the NSIA regime from the screening regimes of other countries, which can be aptly characterised as foreign direct investment regimes given their much greater willingness, on the whole, to exempt deals which involve only domestic parties or else concern designated "White List" (aka "friendly") investors. However, for all this apparent agnosticism, it is becoming clear that BEIS is particularly focusing on deals which involve Chinese acquirers. Indeed, four out of the five prohibition decisions to date have involved investors which are either themselves, or are ultimately owned/controlled by, entities from the Peoples' Republic of China ("**PRC**"). Such heightened focus on PRC-related transactions in the UK by BEIS has even prompted the Chinese embassy to request that the UK provide a "*fair and non-discriminatory environment*" for PRC investors and businesses. Ultimately, we do not know how many deals involving Chinese investors have been scrutinised by BEIS and it is possible that this emerging pattern could simply reflect an increased willingness of Chinese companies to invest in the UK economy. Nonetheless, it seems reasonable to conclude that BEIS is scrutinising Chinese, and even Russian, investments more closely. This dual focus on Russian investors was demonstrated in BEIS' most recently issued prohibition decision, where the presence of Russian oligarch shareholders upstream in the acquirer group – i.e., not the acquirer itself, but its ultimate beneficial owners/individual shareholders – was the element that, according to BEIS, raised the relevant national security concerns.

5 Broad remedies imposed…

As mentioned, during 2022, nine transactions were cleared conditionally. The remedies imposed by BEIS on parties have been extensive, and to date have largely consisted of behavioural remedies (albeit BEIS has the power to impose structural conditions also). The conditions have ranged from and included: (i) the appointment of a government observer to the board of a target's UK subsidiary; (ii) restricting access to sensitive information, technology or IP between the target and acquirer (or other third parties); (iii) preventing the re-location of certain strategic capabilities and operations outside the UK; and (iv) requiring parties to notify, and sometimes obtain consent for, the sale of certain assets.[10] Above all, what is apparent from the conditions imposed to date is that one of BEIS' primary concerns is controlling the flow of certain (confidential) information between the target and the acquirer and ensuring that, post-transaction, the target has adequate security measures in place to prevent unauthorised access to such data by the acquirer (e.g., firewalls). Importantly, in the realm of remedies, it appears that BEIS is not inclined to actively engage in remedy discussions and there is no public consultation of the terms of any final order (as compared to most merger control regimes). Indeed, there is a lack of transparency as to why certain remedies are acceptable, whilst others are not.[11]

[10] See footnote 6.

[11] For instance, the UK Government blocked the *Nexperia/Newport Wafer Fab* acquisition and Nexperia BV noted publicly that the "*far-reaching remedies which Nexperia offered to fully address the Government's concerns have been entirely ignored".*

6 Sectors in the spotlight…?

Although BEIS has investigated deals across a range of sectors, certain ones have been more prominent than others such as defence, military and dual-use, energy, critical suppliers to government, satellite and space technology, communications, advanced materials and data infrastructure. Indeed, BEIS has paid particular attention to deals involving the supply of microchips and/or semiconductor technology. This trend is not surprising given the ongoing global geopolitical tensions on this issue, many of which originate from burgeoning national protectionism and the perceived need to prevent these critical products (and the technology underpinning them) from falling into Chinese ownership. Many countries (including the UK) are wary of the greater competition internationally for products incorporating

semiconductors and the risks that global shortages in semiconductors can pose to an entire country's economy. As a result, many countries – the US perhaps most of all – are seeking to become more self-reliant in this area, and BEIS appears to be similarly motivated. In fact, on the subject of U.S. fears, it is perhaps worth noting how, in response to the Chinese-owned Nexperia's acquisition of Newport Wafer Fab, the U.S. House of Representatives published an open letter urging President Joe Biden to use "all tools necessary" to ensure the deal was retrospectively blocked in the UK.[12] Such a development emphasises not just how much of a focus semiconductors will be for BEIS and other regulators going forwards, but also how BEIS' areas of concern may well be led (at least to a degree) by international geopolitics. The above notwithstanding, deal parties will perhaps be comforted by the fact that none of the deals called in for review in 2022 involved economic areas outside the 17 key sensitive sectors specified by the NSIA's mandatory regime. This suggests that the Government has, in its designation of these key sectors, correctly identified those which are most likely to raise potential national security risks.

7 Are 'national security' grounds or other considerations at the fore…?

The NSIA legislation does not provide any exact definition of the term "national security". This is deliberate given that the UK Government does not, on the one hand, wish to tie its hands by adopting a definition that may quickly become obsolete (given national security concerns are so prone to change), but also, on the other hand, to avoid disclosing those areas of most concern from a national security point for fear that to do so would inform hostile actors where to focus their attention. Therefore, parties will not receive a document setting out BEIS' concerns equivalent to a Statement of Objections or Issues Statement in a competition or merger control investigation. This, again, seems like a reasonable stance and the UK is not alone in such an approach. However, interestingly, there have increasingly been suggestions that the UK Government may be using its broad powers conferred under the NSIA to address other issues, including those relating to industrial policy considerations[13] and others which are not specifically related to any national security risk(s). Given BEIS' increased screening of investments and the lack of transparency as to why certain deals raise concerns, nor why certain partners are deemed unsuitable investors and why certain remedies are acceptable (or not), parties should take this development into account and monitor what seem to be the UK Government's broader concerns going forward. This may help to augur BEIS' future approach to NSIA reviews.

8 Submission of notifications through BEIS' on-line system is cumbersome and challenging…

The information required by the online filing forms (for both the mandatory and voluntary notification regimes) is relatively straightforward, focusing primarily on the business activities of the parties and the acquirer's ultimate beneficial owners. There is no need to even explain the reasons why the proposed

[12] See the open letter at: https://foreignaffairs.house.gov/wp-content/uploads/2022/04/Letter-to-Biden-re-NWF.pdf

[13] For instance, in *Viasat/Immarsat*, BEIS imposed conditions akin to economic undertakings which required Immarsat to expand the number of highly skilled jobs in designated key areas and increase its overall research and development spending in the UK by 30 per cent.

acquisition raises no national security risks, especially in more straightforward cases – albeit it is helpful to add optional information about the rationale and benefits of the deal, which can limit the risk of receiving extensive questions from BEIS and increase parties' chances of securing a clearance swiftly. However, the online filing system can be cumbersome. It applies strict word limits and does not allow for punctuation, making it difficult to describe substantive issues where relevant. The form is also not practically designed for private equity structures or for situations where parties want to make a joint notification.

9 Lack of openness and transparency...

Despite large efforts by BEIS to produce helpful guidance to assist parties to interpret the NSIA and understand how aspects of the regime should operate in practice, there remains a degree of uncertainty about the application of the NSIA and parties are still finding it difficult to navigate the rules. This is not helped by the fact that parties are not able to formally engage with BEIS, although there appear to be cases where BEIS is prepared to discuss "borderline" filings and determine whether a mandatory filing is truly necessary. Otherwise, for simple cases, BEIS does not appoint a case handler, does not provide an email address or phone number for parties to contact and does not update parties on the progress of their case (even when directly asked). This is contrary to other regimes, such as merger control, where parties can meaningfully engage with the regulator on substantive matters pertaining to their case. BEIS also publishes limited information on deals where it has identified national security concerns. It does not, for instance, publish decisions in full (or even flesh out concerns it has identified), but merely makes final orders (i.e., an order imposing a remedy or blocking a deal). Final orders are documents which generally are only one or two pages long and which only provide a high-level description of the national security concerns identified and which have prompted the issuance of the final order. This makes it difficult for parties to understand BEIS' decision-making rationale and procedures, which, in turn, makes the process of bringing any appeal still more difficult (see point 10 below).

10 Appeals on the horizon...or could they face an insuperable challenge...?

The NSIA has been intentionally constructed to make it very difficult to bring an appeal of any decision taken by BEIS. The waters here are likely to soon be tested given that Nexperia has announced its intention to appeal BEIS' decision to retrospectively block its acquisition of Newport Wafer Fab. But parties (including Nexperia) are likely to face an uphill battle (if such an appeal is indeed ultimately lodged). The NSIA regime has two main hinderances which make it very difficult for parties to appeal any prohibition or remedies decision: (1) parties are not provided with a fully reasoned decision and have very little to work with when attempting to rebut BEIS' stated position; and (2) the NSIA does not allow appeals to brought on the substantive elements of BEIS' decisions, but rather only on judicial review grounds which are limited.[14] Indeed, case law indicates that the courts are most reluctant to opine on any issue relating to national security, where they have historically deferred to the Government's own judgement as to what is and is not such a concern. This can be seen, for instance, in judicial reviews of cases involving the deportation of foreign nationals where the basis for doing so (in the Government's view) consisted of, or at least included, reasons of national security. For this reason, it is likely that NSIA appeals will face severe challenges if they relate, at their heart, to the issue as to whether BEIS was justified in making a finding of national security concerns. It will be very interesting, therefore, to see whether Nexperia's

[14] There are four main grounds for making an appeal on judicial review grounds: (1) illegality, where a public body (in this case, BEIS) has acted *ultra vires*; (2) irrationality/unreasonableness, where it will need to be established that BEIS acted contrary to all reasonable logic and precedent (which will be a particularly high bar, given the courts have historically deferred to the Government on issues of national security); (3) procedural impropriety, where BEIS breached some key element of the NSIA review process to the detriment of the relevant party(ies)' rights of defence; and (iv) where BEIS' decision effectively, or actually, affects the party(ies)' human rights.

appeal (the first appeal of its kind vis-à-vis an NSIA final order) will achieve any degree of success. It will undoubtedly set an important precedent for any future appeals.

Final comments

Given how active and interventionist BEIS has been in its first year of operation, parties should take the NSIA very seriously. Parties should consider the timing impact and uncertainty that an NSIA review process can entail and the severe penalties that can be imposed for any failure to notify. Early engagement and submitting clear and thorough notifications should hopefully ensure a relatively smooth and painless process.

BEIS is due to publish its second[15] annual report on the NSIA regime after 31 March 2023, which shall give a better insight into the proportion and types of transactions being reviewed by BEIS, as well as the timing implications of its review process for deal parties. Watch this space…

Contact us

Should you have any queries or wish to discuss any matter in this briefing, please do not hesitate to contact the Competition Team.

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[15] BEIS' first annual report was published on 16 June 2022, albeit this report only covered the first three months of the NSIA regime. BEIS next upcoming report will likely provide a significant amount of insight into the effectiveness and operation of the NSIA regime to date.