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The National Security and Investment Act 2021 – One Year On

Background

The UK's National Security and Investment Act 2021 ("NSIA") came into force one year ago on 4 January 2022. It set out a regime allowing the Secretary of State ("SoS") for Business, Energy and Industrial Strategy in the UK ("BEIS") to potentially block or intervene in acquisitions and investments in any of 17 sectors deemed sensitive from a national security standpoint (including data infrastructure, defence, energy, transport and artificial intelligence).

The regime reflects a global trend for more intervention in national security issues (as shown by the EU FDI Regulation) and requires prior approval to be given to transactions falling within the mandatory notification criteria.

The legislation has wide application, catching qualifying transactions where over 25% of shares, voting rights or material influence in respect of a qualifying business or qualifying assets changes hands (even within existing shareholder bases and groups). It can also potentially apply to lending transactions and to the appointment of a liquidator or receiver.

In addition to a mandatory notification and prior approval requirement for qualifying transactions in those 17 specified sectors, the legislation allows voluntary notifications to be made by parties who wish to avoid deals being called-in by the SoS for scrutiny retrospectively. It also contains call-in powers to allow relevant transactions that were entered into or completed on or after 12 November 2020 to be reviewed.

Failure to comply with NSIA can result in heavy sanctions including turnover-based fines and criminal prosecution, as well as the risk of transactions being void for failure to comply with mandatory notification requirements.

To date, the only acquisitions to be blocked involved Chinese acquirors, but the impact of NSIA has been felt acutely in M&A and private equity transactions in the last year. Parties and advisors have had to get to grips with the additional due diligence workstreams, trigger events, notification process and knock-on effects on timetabling and deal process.

Key Points:

- Failure to comply with NSIA can result in heavy sanctions including turnover-based fines and criminal prosecution, as well as the risk of transactions being void for failure to comply with mandatory notification requirements.
- Consideration of NSIA should form part of the first phase of due diligence in order to minimise delays in the deal timetable and correctly set the expectations of the parties on when a transaction can be completed if a mandatory notification is required.

Notifications and Call-in

Mandatory Notification:

If it is established that prior authorisation from the Investment Security Unit ("ISU") is required for a transaction that falls within the mandatory notification regime, an application must be made via an online portal before the transaction is completed.

Once a notification is correctly submitted to ISU there is an initial 30 working day review period, with most cases being dealt with within this period. The assessment period can be extended by up to 45 working days by the ISU, or longer with acquirer consent. Guidance is available from BEIS on how to correctly fill out the application. The most common reasons for rejection of mandatory notifications are that they should have been voluntary notifications, or that insufficient information on the acquiring entity has been provided.

At present, the ability to interact with the ISU's review team is very limited and there is no list of approved acquiring entities. Creating a register of approved acquiring entities may help to reduce transaction delay and avoid unnecessary applications and cost for active acquirers whose investor base remains unchanged.

In competitive bid situations we have seen multiple bidders submitting mandatory notifications ahead of being selected as preferred bidders with the intention of later withdrawing those submissions. This practice may provide a competitive edge on timetable, or at least the illusion of it at the bid stage but is also likely to result in many unnecessary notifications clogging the ISU's review system and therefore we expect this practice to be looked at by the ISU in due course.

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Voluntary Notification:

If an acquisition or investment does not meet the thresholds for mandatory notification, it can be completed without prior approval. However, the Government has stated that it will encourage voluntary notifications where the transaction could give rise to security concerns.

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"Call-in" Powers:

The SoS has the power to "call-in" any transaction in order to assess its risk to national security. This "call-in" power can be exercised for up to six months after the BEIS becomes aware of the transaction if it is within five years after completion of the transaction. As this power is retrospective, any relevant transactions entered into from 12 November 2020 may also potentially be called-in. When determining whether to "call-in" a transaction the SoS must have regard to the following:

- **Target Risk** – the nature and activities of the target;
- **Control Risk** – the type and level of control being acquired; and
- **Acquirer Risk** – the extent to which the acquirer raises national security concerns.

NSIA does not set out the factors it will consider in respect of the above, nor does it define "national security" as mentioned above. By leaving the same undefined, the Government can remain flexible and free to call in deals at its discretion, however, factors such as the ultimate beneficial owners of an acquirer, any links to sanctioned person or territories and any potential links to criminal activity will of course be considered.

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Impact of NSIA on Loan Facilities

The granting of a loan or taking of security by a lender is not expected to trigger the application of the NSIA, unless:

- The loan or security arrangement gives the lender the ability to exercise "material influence" over the borrower. Material influence in this context means that the rights afforded to the lender would go beyond the standard undertakings and enable the lender to materially influence policy relevant to the borrower's behaviour in the market.

- The loan or security arrangement gives the lender the right to take ownership of the shares, and/or the ability to exercise or direct voting rights. The BEIS has issued guidance on this point to clarify that the mandatory regime is triggered at the enforcement stage where title to the shares is not transferred to the secured lender upon granting the share charge. However, care is required in the context of automatic enforcement provisions.

- The loan or security arrangement involves the granting of security over assets (other than shares), which involves a transfer of title or gives rights to the lender to use the asset, or control how the asset is used during the security period.

All the above instances can give rise to a "call-in" by the SoS and it is sensible to pay particular attention to these potential triggers during the drafting stage of any relevant transaction.

Key Learning Points from the NSIA's First Year

Consideration of NSIA should form part of the first phase of due diligence in order to minimise delays in the deal timetable and correctly set the expectations of the parties on when a transaction can be completed if a mandatory notification is required.

In terms of deal structuring, if a mandatory notification is required, it may drive parties to exchange and close conditional upon receipt of NSIA approval, which is important to factor into deal mechanics and timetabling from the outset.

Whilst the responsibility for assessing whether NSIA will apply to a deal will fall on the transacting parties, given the possible issues arising from non-compliance with the regime, it may also be in the best interest of lenders to also carry out their own due diligence or pursue a legal opinion in respect of the application of NSIA and/or to make completion of their facility conditional upon obtaining NSIA approval.

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Guidance:

If you require further information about anything covered in this briefing, please contact **Vicky Dummigan** or your usual contact at the firm on **+44 (0)28 9099 8207**. This publication is not designed to provide legal or other advice and does not deal with every important topic or cover every aspect of the topics with which it deals. Publication date: January 2023.

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