

# UK Proposes Increased Scrutiny of Foreign Investments on National Security Grounds

27 July 2018

The UK Government Department for Business, Energy and Industrial Strategy has launched a consultation proposing reforms designed to strengthen its powers to protect national security in acquisitions of assets or entities by foreign investors. The proposals aim to bring the UK's foreign investment regime closer in line with those of other countries, including the United States, France and Germany, which would significantly increase the number of Government interventions in acquisitions by foreign investors.

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The regime would be used by the Government to determine whether to approve, approve with conditions, block or unwind transactions that present national security risks.

Responses to the consultation are required by 16 October 2018, but no fixed time frame has been set for the introduction of any primary legislation.

**The system in effect today.** Currently, under the Enterprise Act 2002, the Government can intervene in a transaction on national security grounds in three circumstances:

- if it has been notified to the European Commission under the EU Merger Regulation,
- where the business being acquired has UK turnover of more than £70 million (or, from May 2018, in the case of dual use and military use, quantum and computing hardware technologies, more than £1 million), or the parties have a combined market share of 25%, or
- in respect of mergers that do not meet such thresholds but which involve a party designated as a relevant Government contractor.

Purchases of assets such as intellectual property fall outside the scope of the current law. The Government currently intervenes in approximately one case per year on grounds of national security and believes that its powers under the Enterprise Act 2002 are no longer sufficient to address the challenging and changing national security threats faced by the UK.

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**The proposals.** The proposals laid out in the Government's White Paper (National Security and Investment—A consultation on proposed legislative reforms)<sup>1</sup> represent a significant shift away from the current regime towards a formal foreign investment review process. This follows a recent trend across Europe (including in Germany<sup>2</sup> and France, as well as at EU level<sup>3</sup>) and is being considered also in the context of the Committee on Foreign Investment in the United States potentially tightening its rules on foreign investments. It has been widely reported that these proposals are being made in light of buyers linked to foreign governments (including Chinese buyers) acquiring sensitive assets and businesses. The proposals are something of a reversal of a long-term trend in British government policy since the 1980s which has seen intervention as something that should happen only exceptionally.

The UK Government is proposing full reform of the existing notification regime under the Enterprise Act 2002 through the introduction of primary legislation. The new law would increase the Government's power to target transactions in which national security is considered to be at risk, irrespective of minimum turnover or market share thresholds. Acquisitions of control or influence over UK entities or assets, including real or personal property, IP rights and contractual rights raising national security concerns across all sectors of the economy would be subject to the new regime. This could include any investment or activity that involves the acquisition of more than 25% of an entity's shares or votes, or significant influence or control over an entity. It would also apply to further acquisitions beyond the foregoing thresholds.

Parties would be encouraged to notify their transaction if they consider that there may be national security concerns, although the Government would reserve the right to intervene, including for a limited period of time post-transaction, where it has not been notified.

**Increased intervention.** The Government expects there to be around 200 notifications made each year under the new regime, and it would aim to quickly screen out (within 15 working days, extendable by a further 15 working days) those cases in which it has no national security concerns. Around half of the notifications (approximately 100 per year) are expected to raise national security concerns, which the Government would subject

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<sup>1</sup> The White Paper is available here:  
[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/728310/20180723\\_-\\_National\\_security\\_and\\_investment\\_-\\_final\\_version\\_for\\_printing\\_1\\_.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/728310/20180723_-_National_security_and_investment_-_final_version_for_printing_1_.pdf).

<sup>2</sup> Our Client Update on the regime in Germany is available here:  
[https://www.debevoise.com/~/\\_media/files/insights/publications/2017/07/20170721\\_germany\\_tightens\\_control\\_over\\_inbound\\_corporate\\_investments.pdf](https://www.debevoise.com/~/_media/files/insights/publications/2017/07/20170721_germany_tightens_control_over_inbound_corporate_investments.pdf).

<sup>3</sup> Our Client Update on the EU regime is available here:  
[https://www.debevoise.com/~/\\_media/files/insights/publications/2017/09/20170925%20auropean%20commission%20calls%20for%20common%20scrutiny%20of%20foreign%20direct%20investments.pdf](https://www.debevoise.com/~/_media/files/insights/publications/2017/09/20170925%20auropean%20commission%20calls%20for%20common%20scrutiny%20of%20foreign%20direct%20investments.pdf).

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to a full assessment process involving a potentially extensive information-gathering exercise. The Government currently proposes an initial period of 30 working days to make its assessment of the national security risks, which it would be able to extend for a further 45 working days where more detailed scrutiny is required. The Government has stated that it will keep this period under review, and it may increase or decrease in the final proposals.

**Imposition of remedies.** If, following its assessment, the Government concludes that national security is at risk, it would have the power to impose remedies. Remedies are expected to be required in around a quarter of all notified cases each year—approximately 50 per year. This would represent a marked increase in the current annual average of one intervention per year.

The Government stresses in its White Paper that available remedies to prevent or mitigate risks to national security should be flexible enough to allow the individual circumstances to be considered and addressed on a case-by-case basis. This would mean empowering senior Government ministers to impose such remedies as they consider necessary to protect national security in the circumstances of each case. The proposed legislation would allow the Government to impose conditions on any party to a transaction, taking any form—an indicative list would be included in the legislation with more details to be set out in legislative guidance. If the Government concludes that no remedy is able to address or mitigate a given risk to national security, it would have the power to block a transaction or unwind it if it has already taken place. The Government's powers under the regime would be subject to an appeals process based on and aligned with judicial review principles and would be heard by the High Court.

**Civil and criminal sanctions for non-compliance.** Strong and clear sanctions in the form of criminal convictions and civil financial penalties are proposed to incentivise compliance and punish breaches of the regime, such as non-compliance with information requests or remedial action imposed by the Government. Custodial sentences of up to five years would be available for most offences, although breaches of some information-gathering requirements would attract lesser sanctions. Financial penalties could be imposed upon both individuals and businesses as an alternative to pursuing criminal convictions, and directors may also be disqualified instead of, or in addition to, other sanctions.

**Careful implementation required.** A careful and thorough process to ensure that the proposed reforms interact with other regimes, such as the UK competition regime, the Takeover Code and the EU framework of directives and regulations, including EU merger regulations and forthcoming EU Foreign Direct Investment Screening Regulation (for so long as the UK remains a member of the EU), would need to be undertaken prior to the introduction of any primary legislation.

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In light of the Government's packed legislative programme, it is not possible to predict whether or when these proposals will be implemented, but the impact on cross-border investment into the UK could be significant. We will provide further updates as they become available. In the meantime, if you have any questions, please contact one of the authors of this update or your usual Debevoise contact.

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