UK Expands Foreign Investment Rules in Response to COVID-19

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SUMMARY

From 23 June, the UK government is able to intervene in M&A deals to ensure they do not threaten the United Kingdom's ability to combat a public health emergency. The new powers enable the government to intervene if a business that is directly involved in a pandemic response (for example, a vaccine research company or personal protective equipment manufacturer) finds itself the target of an approach. There is sufficient ambiguity in what that may mean in practice that the rules could potentially be applied widely across the healthcare, pharmaceutical, manufacturing and food supply chain sectors. In addition, the government will have expanded powers to scrutinise and intervene in deals affecting certain key technology sectors considered central to national security.

CURRENT POWERS

Under the current UK legislation, there is no formal distinction between domestic and foreign investment. Instead, the UK government can intervene and review a transaction on "public interest" grounds if it meets the merger control thresholds. The UK thresholds are generally based on the share of supply (*i.e.*, the transaction creates or enhances a 25% share of supply or purchases in the United Kingdom) or turnover (the target's UK turnover exceeds £70 million). Since 2018, if the transaction involves the military and dual use, multipurpose computing hardware or quantum technology sectors, the relevant turnover threshold is lowered to £1 million and the share of supply test can be satisfied by the target alone.

The current public interest grounds are national security and defence, plurality of the media and regulation of the UK financial system. In practice, such interventions have historically been more likely for national security reasons, particularly if a transaction involves a foreign investor. Since 2002, the government has intervened in 20 deals, 12 of which were due to national security concerns. There has been a recent increase in the government's appetite to step in, however, and four of those public interest interventions were in 2019. The only ongoing one of those is in relation to the (now abandoned) proposed takeover of the UK-based engineering company Impcross Limited by Gardner Aerospace Holdings Limited, a Chinese-owned aerospace firm. Although no deal has technically ever been blocked, it is very common for the acquirer to have to offer concessions to get approval.

NEW PROTECTIONS

The two changes are:

- **New Public Interest Ground for Review** – There is a new public interest ground on the basis of which the UK government can intervene in transactions where there is "*the need to maintain* […] *the capability to combat, and to mitigate the effects of, public health emergencies*". In practice, this new trigger is broad enough to encompass many sectors, including healthcare, pharmaceutical and medical equipment manufacturing as well as the food supply chain and related logistics. This change came into force on 23 June.

- **Lower Threshold for Review** – The second change sets out three specific sectors that will fall within the lower turnover threshold under the current merger control rules. The sectors are artificial intelligence, advanced materials and cryptographic authentication technology. As a result, the relevant turnover threshold for transactions involving these sectors is £1 million and the share of supply test can be satisfied by the target alone. This change is expected to come into force this week, once the relevant secondary legislation has been approved by the UK Parliament.

NEXT STEPS

The UK government has been considering its approach to screening foreign investments for some time and these most recent changes build on similar sectoral changes introduced in 2018. The UK government's press release makes it clear, however, that this is a stopgap measure to mitigate the risks of predatory M&A during the Covid-19 pandemic. The UK government is still intending to implement the wider-ranging reforms already announced in December 2019 that will strengthen its existing powers to scrutinise and intervene in transactions in order to protect national security.

The proposed National Security and Investment Bill is expected to become law later in 2020 and will introduce a notification system, possibly similar to CFIUS in the United States, requiring businesses to flag transactions that may give rise to national security concerns. That will involve a comprehensive overhaul of the United Kingdom's rules by introducing a foreign investment screening regime separate from the current merger control regime, meaning that it would apply across all sectors and to businesses of any size (regardless of turnover or market share). As such, the United Kingdom will join other major jurisdictions, including the European Union and various of its Member States, that have recently enhanced and expanded their ability to regulate foreign investment.

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For more information regarding the legal impacts of the coronavirus, please visit our Coronavirus Resource Center.

Please do not hesitate to contact us with any questions.

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