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New mandatory notification regime for transactions in the UK

The UK has introduced new legislation that requires transactions in certain sectors to be approved by the UK government before they can be completed.

FOR WHAT MATTERS

A new regime

The UK has introduced a new regime which, from 4 January 2022, requires prior approval for transactions in certain specified sectors. Many of the sectors are technology-focused and attractive to venture capital investors. The new regime, contained in the National Security & Investment Act 2021, also gives the UK government the ability to "call in" for review on national security grounds transactions in all sectors of the economy (with the government having the ability retrospectively to review transactions that have taken place since 12 November 2020). It is likely to have significant implications for VCs and their portfolio companies, most likely upon exit but potentially also in respect of investments into those companies.

The new regime is very broad and affects many transactions. In outline:

- **There are 17 sectors for which prior approval is required.** These are listed in the table below. They include communication, artificial intelligence, computer hardware, data infrastructure, defence, energy and transport. The definitions of these sectors are broad.

- **There are no materiality thresholds.** If the target has any activities (no matter how big or small) in the UK in one or more of the specified sectors, prior approval will be required.

- **Transactions are caught by the regime where control over the target is acquired, but the test for control is very low.** The test is met, for example, by any shareholding over 25% (as well as by certain increases in shareholding thereafter), so could apply to investments as well as exits

- **Whilst the regime is intended to enable the UK government to review deals on national security grounds, transactions in the specified sectors require approval regardless of whether they give rise to any national security issues.** The government estimates that around 1,800 deals will be notified for approval each year, of which only a very small proportion will give rise to any concerns.

- **Failure to obtain approval will render the transaction void and may constitute a criminal offence by the investor/purchaser (and potentially also by its officers).** In practice, any failure to obtain approval may also lead to commercial challenges on future investments or acquisitions involving the same target (for example, in the event of an exit by the investor).

- **Where a transaction gives rise to national security concerns, the UK government has extensive powers to take steps to address those concerns.**

Shoosmiths’ views

Since the new regime came into force in January 2022, we have advised on a significant number of deals under the new rules. We are therefore well placed to assess the impact of this new regime. Our key observations include:

- **The impact of this new regime will be significant – any acquisition of a stake exceeding 25% should be considered carefully to establish whether approval is required.** As indicated above, the government estimates that around 1,800 transactions will be notified for approval each year.
- **Describing the regime as a “national security” one is to some extent misleading - most deals that require approval do not give rise to any national security considerations at all.** Whilst the purpose of the regime is to enable the UK government to screen transactions for national security concerns, most transactions that require prior approval will very clearly not give rise to any national security concerns but will require approval simply because the target is active in one of the 17 sectors (which, again, are broadly defined).
- **It is crucial that parties and their advisers take appropriate care to establish whether approval is required – the consequences of getting it wrong are potentially significant.** Aside from the risk of criminal sanctions, any failure to obtain approval is likely to cause complications in any future sale process involving the target (and is likely to be picked up by prospective purchasers in due diligence) given that it will render the transaction void.
- **When conducting due diligence on transactions, it will be important to establish whether any previous (post 4 January 2022) transactions involving the target should have been approved under the regime.** If the target was the subject of a previous transaction that should have been approved, but was not, that would render the transaction in question void (which could have obvious repercussions for subsequent purchasers of the business).
- **Where a deal requires approval, the notification and approval process is relatively straightforward.** Deals that do not give rise to any national security issues should be approved within 30 working days (and in practice, often a few days sooner).
- **Importantly, the new regime is not intended to deter investment in UK businesses.** Whilst the regime will enhance the UK government’s ability to monitor and review transactions from a national security perspective, the expectation is that it expresses concerns about only a very small number of deals each year.

We would, of course, be very happy also to support you on any transactions in which the target has activities in the UK and where the new regime might apply.

The 17 sectors for which there will be mandatory prior approval are:

- Advanced Materials
- Advanced Robotics
- Artificial Intelligence
- Civil Nuclear
- Communications
- Computing Hardware
- Critical Suppliers to Government
- Cryptographic Authentication
- Data Infrastructure
- Defence
- Energy
- Military and Dual-Use
- Quantum Technologies
- Satellite and Space Technologies
- Suppliers to the Emergency Services
- Synthetic Biology
- Transport (ports, harbours and airports)

The mandatory prior approval regime will apply where the target has activities in the UK in one or more of the above sectors. Note that the precise scope of each sector is set out in accompanying definitions, the scope of which can be very broad.

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