The City of London Law Society

The Law Society

House of Commons Public Bill Committee
National Security and Investment Bill 2019-21

Written evidence submitted by the Company Law Committees of the City of London Law Society and the Law Society of England and Wales (NSIB03)

A Joint Working Party (the ***Committee***) of the Company Law Committees of the City of London Law Society (***CLLS***) and the Law Society of England and Wales (the ***Law Society***) has reviewed the proposed national security and investment regime (the ***proposed regime***) set out in the National Security and Investment Bill (the ***Bill***) and associated documents.

The CLLS represents approximately 17,000 City lawyers through individual and corporate membership, including some of the largest international law firms in the world. The Law Society is the professional body for solicitors in England and Wales, representing over 170,000 registered legal practitioners. The Committee is made up of senior and specialist corporate lawyers from both the CLLS and the Law Society who have a particular focus on issues relating to mergers and acquisitions and inbound investment.

The Committee has prepared a paper, which accompanies this letter, summarising its principal views on the proposed regime.

The Committee understands and supports the Government's objective to protect national security from hostile foreign actors. However, as the Government has noted in the published materials which accompanied the Bill, investment – both domestic and foreign – makes a vital contribution to the UK economy and there are a small number of transactions which may pose a risk to national security.

It is very important for the UK that the proposed regime does not, on account of this small number of hostile transactions, deter the very wide range of beneficial investment in the UK or undermine clarity and predictability for investors.

The Committee has significant concerns in relation to the scope and technical detail of the Bill and as to the operation of the Bill in practice and is concerned that the proposed regime as currently proposed would have an adverse impact on the attractiveness of the UK for inbound investment. For instance, the Committee has identified potentially materially adverse effects on public market transactions involving listed companies (such as Takeover Code transactions and capital raisings), foreign investment by pension funds and sovereign wealth funds (which is particularly important in UK infrastructure projects), the efficient functioning of the London loan market, passive investments in private equity and venture capital funds, investment in key sectors in the UK (such as the technology sector) and on passive foreign investment, which has been providing much needed liquidity to UK companies in the current challenging economic conditions. The breadth of the proposed regime also goes beyond comparable regimes in other developed economies such as the US and Australia. Certain of the key concerns identified by the Committee are summarised in the attached table and described in further detail in the accompanying paper.

The Committee believes that there are implementable solutions in relation to the concerns which it has identified and wishes to put forward proposed solutions to create a better balanced regime. These proposed solutions are set out in a series of recommendations for narrowing the scope of the proposed regime in certain key areas in order to promote greater certainty and predictability but without undermining the key aims of the proposed regime. Those recommendations are summarised in the attached table and set out in further detail in the accompanying paper.

The Committee has also identified a number of concerns with some of the detail of the proposed regime and intends separately to share suggested drafting changes to address these concerns.

We would welcome an opportunity to discuss any questions you might have on the concerns we have raised and/or the recommendations we have put forward. Please feel free to contact Sam Bagot (sbagot@cgsh.com) or David Pudge (david.pudge@cliffordchance.com).

For and on behalf of

The City of London Law Society Company Law Committee

The Law Society of England and Wales Company Law Committee

2nd December 2020

NATIONAL SECURITY AND INVESTMENT BILL – SUMMARY OF KEY POINTS[1]

Topic	*Position in Bill (and associated documents)*	*Committee comments / proposals*
1. Context	While investment – both domestic and foreign – makes a vital contribution to the UK economy, a small number of investment activities have the potential to pose a risk to national security.	• The UK seeks to be an open and transparent economy and an international trading centre. It is in a different position from other countries (for instance, the resource based economies) which have adopted similar regimes. It is vital that the UK does not end up with a regime which adversely impacts investor confidence – otherwise investors will go elsewhere. • The Committee believes that the scope of the proposed regime is disproportionate in light of the small number of transactions which may give rise to national security concerns and will undermine foreign investment in the UK. • Changes to the proposed regime should be made to significantly reduce its scope and to promote certainty and predictability. The Committee believes that the recommendations set out below achieve this without undermining the key goals of the proposed regime.
2. Meaning of National Security and call in power	The term "national security" is not defined in the Bill. The draft Statement of Policy Intent gives certain guidance on the circumstances in which the call in power may be exercised.	• The clarity and predictability of proposed regime will be undermined if it is, or is seen to be, politicised particularly as the Government changes over time. • Recommendations: (1) At a minimum, the Bill should clearly state what "national security" is not: it should be clear that this is distinct from "national interest" and the powers under the proposed regime will not be exercised for the purposes of industrial policy, short term political expediency, other political or economic reasons (such as safe-guarding jobs in the UK) or in a manner which would undermine the legitimate benefits of foreign investment in the UK. (2) In order to promote clarity, the proposed regime should provide that the call-in power will only be exercised when all three risks (acquirer, target and trigger event risks) are present.
3. Scope of the mandatory regime	Mandatory notification is required in respect of transactions in 17 sectors defined in the draft secondary legislation.	• The combination of the broad definition of sectors subject to mandatory notification, the scope of the remedies (see below), the absence of a de minimis (see below) and the very broad foreign nexus provisions (see below) will force investors to take a safety first approach and either make filings or seek informal guidance. This will lead to the Government being inundated with filings and requests for guidance particularly on commencement of the proposed regime and more generally have an adverse impact on UK investment. • Recommendation: The scope of the 17 sectors the subject of the mandatory notification regime is excessive and should be cut back. In particular, certain of the sectors (such as artificial intelligence and communications) are defined so broadly that they could catch almost any business. This should be a key focus on the ongoing consultation on the relevant secondary legislation.
4. Scope of remedies	A notifiable acquisition is "void" if not approved before completion.	• This is inconsistent with the concept in the Bill of making a retrospective approval application. It will give rise to significant uncertainty, and it is likely to be unworkable, for such transactions to be deemed "void".

[1] This table summarises certain of the key comments and proposals made by a Joint Working Party (the ***Committee***) of the Company Law Committees of the City of London Law Society (***CLLS***) and the Law Society of England and Wales (the ***Law Society***) in relation to the proposed national security and investment regime (the ***proposed regime***) set out in the National Security and Investment Bill (the ***Bill***) and associated documents. Please refer to the Committee's paper on the Bill and associated documents for more context.

Topic	Position in Bill (and associated documents)	Committee comments / proposals
		• <u>Recommendations</u>: (1) The proposed regime should provide that: (a) interim orders and forced sales by the buyer to an appropriate third party will suffice in almost all cases; and (b) only as a last resort when other remedies are not possible, transactions will be "voidable", not "void". (2) In addition, it would seem exceptionally difficult and unfair to "void" or avoid (unwind) listed company public market transactions involving public market (including retail) investors. The Government should therefore provide an appropriate exemption (or safe harbour) from these remedies in relation to transactions subject to the Takeover Code and certain capital markets transactions involving listed companies (such as underwriting arrangements for placings and rights issues).
<u>5. Foreign/UK nexus</u>	Transactions relating to the following are subject to the proposed regime: • entities formed outside of the UK if they supply goods or services to persons in the UK; and • assets located outside of the UK if used in connection with supply of goods or services in UK.	• The extra-territorial scope of the proposed regime makes the UK a significant outlier (compared with regimes in Australia, Canada, France, Germany, Spain or the United States) and is disproportionate. Investors in a broad range of foreign business would have to perform extensive due diligence to determine if any goods or services are supplied directly or indirectly into the UK. • <u>Recommendations</u>: The proposed regime should apply only to the acquisition of UK entities and assets located in the UK. Specific concerns relating to off-shore assets should be dealt with through other regulation.
	Domestic acquirers are subject to the proposed regime	It is unnecessary and disproportionate to have UK acquirers in scope; other established regimes (e.g., Australia and United States) do not apply to domestic acquirers.
<u>6. Absence of *de minimis* for small transactions</u>	The Bill does not contain a *de minimis* threshold for small transactions.	• It is disproportionate for the proposed regime to apply to transactions which are very small and unlikely to give rise to national security concerns. The Committee is particularly concerned about the impact on the UK tech sector. • <u>Recommendation</u>: The Bill should introduce a *de minimis* threshold for the mandatory notification regime (or at least sector specific thresholds for each of the 17 sectors the subject of the mandatory notification regime). This would still leave the Secretary of State with discretion to be able to call-in certain transactions that are of specific concern.
<u>7. Safe harbours and guidance</u>	The proposed regime does not contain safe harbours in relation to the matters referred to opposite. This undermines clarity and predictability.	<u>Recommendations</u>: The proposed regime should introduce specific safe harbours for: 1. customary minority investment rights; 2. passive investments in private equity and venture capital funds; and 3. certain types of investors (such as investors from particular jurisdictions, regulated banks, investors with a pre-existing track record and investors with certain other characteristics such as retail investment funds).
	The Statement of Policy Intent provides that, although the overwhelming majority of loans are not expected to pose a threat to national security, loans are not exempt from the proposed regime	• Subjecting loans to the proposed regime – particularly without clarity as to when a loan would be of concern - will cause considerable uncertainty for the London loan market. • <u>Recommendations</u>: Loan agreements documented on LMA standard terms or substantially similar terms should be benefit from a safe-harbour. Debt securities and derivatives should benefit from a complete exemption from the proposed regime.

Topic	*Position in Bill (and associated documents)*	*Committee comments / proposals*
	The Statement of Policy Intent gives helpful guidance but it is not sufficient on its own.	Recommendations: • The new Government unit should be appropriately staffed to deal with a much higher number of filings and requests for guidance than the Government is currently anticipating. • Further guidance should be made available to the market including through an annual review and other guidance issued from time to time after material developments. Further detail is given in the longer paper.
8. Transitional regime	The proposed regime has retrospective effect to transactions which close after 12 November 2020 but before the commencement of the Bill.	• The proposed retrospective effect will give rise to considerable uncertainty for transactions closing after 12 November 2020. • Recommendations: (1) Transactions signed before 12 November 2020 should be exempt from the proposed regime. (2) Other transactions which close after 12 November 2020 should benefit from a safe harbour if they have been pre-vetted by BEIS.

National Security and Investment Bill

Joint Response of the Company Law Committees of the City of London Law Society and the Law Society

2 December 2020

JOINT RESPONSE OF THE COMPANY LAW COMMITEES OF THE LAW SOCIETY AND THE CITY OF LONDON LAW SOCIETY TO THE NATIONAL SECURITY AND INVESTMENT BILL AND ASSOCIATED DOCUMENTS

The views set out in this paper, in relation to the proposed national security and investment regime (the ***proposed regime***) set out in the National Security and Investment Bill (the ***Bill***) and associated documents including the draft Statement of Policy Intent (***SPI***), have been prepared by a Joint Working Party (the ***Committee***) of the Company Law Committees of the City of London Law Society (***CLLS***) and the Law Society of England and Wales (the ***Law Society***). See the annex to this paper for further information relating to the CLLS and the Law Society.

1. EXECUTIVE SUMMARY

The Committee understands and supports the Government's objective to protect national security from hostile foreign actors. However, as the Government has noted in the published materials which accompanied the Bill, investment – both domestic and foreign – makes a vital contribution to the UK economy and there are a small number of transactions which may pose a risk to national security.

The UK is, and seeks to be, an open and transparent economy and an international trading centre. The Government has also spoken of its objective of attracting investment from around the world as the UK embraces new opportunities post-Brexit and it recovers from the coronavirus pandemic. Meanwhile, foreign direct investment in the UK has fallen significantly in recent years.

It is very important for the UK that the proposed regime does not, on account of this small number of hostile transactions, deter the very wide range of beneficial investment in the UK or undermine clarity and predictability for investors.

The Committee has significant concerns in relation to the scope and technical detail of the Bill and as to the operation of the Bill in practice and is concerned that the proposed regime as currently proposed would have an adverse impact on the attractiveness of the UK for inbound investment. For instance, the Committee has identified in this document potentially material adverse effects on public market transactions involving listed companies (such as Takeover Code transactions and capital raisings), foreign investment by pension funds and sovereign wealth funds (which is particularly important in UK infrastructure projects), the efficient functioning of the London loan market, passive investments in private equity and venture capital funds, investment in key sectors in the UK (such as the technology sector) and on passive foreign investment, which has been providing much needed liquidity to UK companies in the current challenging economic conditions.

The breadth of the proposed regime goes beyond comparable regimes in other developed economies such as the US and Australia. Certain of the key concerns identified by the Committee are summarised in the attached table entitled "Executive Summary" and described in further detail in this paper.

The Committee believes that there are implementable solutions in relation to the concerns which it has identified and wishes to put forward proposed solutions to create a better balanced regime. These proposed solutions are set out in a series of recommendations for narrowing the scope of the proposed regime in certain key areas in order to promote greater certainty and predictability but without undermining the key aims of the proposed regime. Those recommendations are summarised in the attached table entitled "Executive Summary" and set out in further detail in this paper.

In addition to the concerns and recommendations set out in this paper, the Committee has various other comments and recommendations (including specific drafting suggestions) on some of the detail of the proposed regime and intends to share these with the Government in due course.

EXECUTIVE SUMMARY

Topic	*Position in Bill (and associated documents)*	*Committee comments / proposals*
1. Context	While investment – both domestic and foreign – makes a vital contribution to the UK economy, a small number of investment activities have the potential to pose a risk to national security.	• The UK seeks to be an open and transparent economy and an international trading centre. It is in a different position from other countries (for instance, the resource based economies) which have adopted similar regimes. It is vital that the UK does not end up with a regime which adversely impacts investor confidence – otherwise investors will go elsewhere. • The Committee believes that the scope of the proposed regime is disproportionate in light of the small number of transactions which may give rise to national security concerns and will undermine foreign investment in the UK. • Changes to the proposed regime should be made to significantly reduce its scope and to promote certainty and predictability. The Committee believes that the recommendations set out below achieve this without undermining the key goals of the proposed regime.
2. Meaning of National Security and call in power	The term "national security" is not defined in the Bill. The draft Statement of Policy Intent gives certain guidance on the circumstances in which the call in power may be exercised.	• The clarity and predictability of proposed regime will be undermined if it is, or is seen to be, politicised particularly as the Government changes over time. • Recommendations: (1) At a minimum, the Bill should clearly state what "national security" is not: it should be clear that this is distinct from "national interest" and the powers under the proposed regime will not be exercised for the purposes of industrial policy, short term political expediency, other political or economic reasons (such as safe-guarding jobs in the UK) or in a manner which would undermine the legitimate benefits of foreign investment in the UK. (2) In order to promote clarity, the proposed regime should provide that the call-in power will only be exercised when all three risks (acquirer, target and trigger event risks) are present.
3. Scope of the mandatory regime	Mandatory notification is required in respect of transactions in 17 sectors defined in the draft secondary legislation.	• The combination of the broad definition of sectors subject to mandatory notification, the scope of the remedies (see below), the absence of a de minimis (see below) and the very broad foreign nexus provisions (see below) will force investors to take a safety first approach and either make filings or seek informal guidance. This will lead to the Government being inundated with filings and requests for guidance and more generally have an adverse impact on UK investment. • Recommendation: The scope of the 17 sectors the subject of the mandatory notification regime is excessive and should be cut back. In particular, certain of the sectors (such as artificial intelligence and communications) are defined so broadly that they could catch almost any business. This should be a key focus on the ongoing consultation on the relevant secondary legislation.
4. Scope of remedies	A notifiable acquisition is "void" if not approved before completion.	• This is inconsistent with the concept in the Bill of making a retrospective approval application. It will give rise to significant uncertainty, and it is likely to be unworkable, for such transactions to be deemed "void". • Recommendations: (1) The proposed regime should provide that: (a) interim orders and forced sales by the buyer to an appropriate third party will suffice in almost all cases; and (b) only as a last resort when other remedies are not possible, transactions will be "voidable", not "void". (2) In addition, it would seem exceptionally difficult and unfair to "void" or avoid (unwind) listed company public market transactions involving public market (including retail) investors. The Government should therefore provide an appropriate exemption (or safe harbour) from these remedies in relation to transactions subject to the

Topic	*Position in Bill (and associated documents)*	*Committee comments / proposals*
		Takeover Code and certain capital markets transactions involving listed companies (such as underwriting arrangements for placings and rights issues).
5. Foreign/UK nexus	Transactions relating to the following are subject to the proposed regime: • entities formed outside of the UK if they supply goods or services to persons in the UK; and • assets located outside of the UK if used in connection with supply of goods or services in UK.	• The extra-territorial scope of the proposed regime makes the UK a significant outlier (compared with regimes in Australia, Canada, France, Germany, Spain or the United States) and is disproportionate. Investors in a broad range of foreign business would have to perform extensive due diligence to determine if any goods or services are supplied directly or indirectly into the UK. • Recommendations: The proposed regime should apply only to acquisition of UK entities and assets located in the UK. Specific concerns relating to off-shore assets should be dealt with through other regulation.
	Domestic acquirers are subject to the proposed regime	It is unnecessary and disproportionate to have UK acquirers in scope; other regimes (e.g., Australia and United States) do not apply to domestic acquirers.
6. Absence of *de minimis* for small transactions	The Bill does not contain a *de minimis* threshold for small transactions.	• It is disproportionate for the proposed regime to apply to transactions which are very small and unlikely to give rise to national security concerns. The Committee is particularly concerned about the impact on the UK tech sector. • Recommendation: The Bill should introduce a *de minimis* threshold for the mandatory notification regime (or at least sector specific thresholds for each of the 17 sectors the subject of the mandatory notification regime). This would still leave the Secretary of State with discretion to be able to call-in certain transactions that are of specific concern.
7. Safe harbours and guidance	The proposed regime does not contain safe harbours in relation to the matters referred to opposite. This undermines clarity and predictability.	Recommendations: The proposed regime should introduce specific safe harbours for: 1. customary minority investment rights; 2. passive investments in private equity and venture capital funds; and 3. certain types of investors (such as investors from particular jurisdictions, regulated banks, investors with a pre-existing record and investors with certain other characteristics such as retail investment funds).
	The Statement of Policy Intent provides that, although the overwhelming majority of loans are not expected to pose a threat to national security, loans are not exempt from the proposed regime	• Subjecting loans to the proposed regime – particularly without clarity as to when a loan would be of concern - will cause considerable uncertainty for the London loan market. • Recommendations: Loan agreements documented on LMA standard terms or substantially similar terms should be benefit from a safe-harbour. Debt securities and derivatives should benefit from a complete exemption from the proposed regime.
	The Statement of Policy Intent gives helpful guidance but it is not sufficient on its own.	Recommendations: • The new Government unit should be appropriately staffed to deal with a much higher number of filings and requests for guidance than the Government is currently anticipating. • Further guidance should be made available to the market including through an annual review and other guidance issued from time to time after material developments. Further detail is given in the longer paper.
8. Transitional regime	The proposed regime has retrospective effect to transactions which close after 12 November 2020 but before the commencement of the Bill.	• The proposed retrospective effect will give rise to considerable uncertainty for transactions closing after 12 November 2020. • Recommendations: (1) Transactions signed before 12 November 2020 should be exempt from the proposed regime. (2) Other transactions which close after 12 November 2020 should benefit from a safe harbour if they have been pre-vetted by BEIS.

2. NATIONAL SECURITY AND CALL IN POWER

2.1 The term "national security" is not defined in the Bill.

2.2 As noted in the House of Commons Library Briefing Paper on the Bill, the danger is that national security (which is undefined) could merge into industrial policy or short term political considerations, particularly as the Government (and Government policy) changes over time. This is particularly the case in view of the fact that the Secretary of State (rather than an independent regulator) will be responsible for reviewing transactions. There has also been a perception that the public interest powers under the Enterprise Act 2002 (***EA 2002***) have, in recent years, been exercised in a manner which has increasingly moved towards industrial policy and political considerations.[1] The Committee is conscious of the fact that cross-border M&A transactions, particularly where the target is a high profile British brand or there are concerns about the potential impact on employment, are often conducted in the glare of media attention giving rise to intense political pressures on Government.

2.3 Clarity and predictability are key features of the UK legal system and this is rightly seen as an attraction of doing business in the UK. These will be undermined if the proposed regime is, or is seen to be, politicised. While other foreign investment regimes have specifically defined "national security"[2], we understand the Government's concern is that national security considerations may potentially be relevant in a number of sectors of the economy. However, in the Committee's view, at a minimum the Bill should clearly state what "national security" is not. That is, the Bill should expressly provide that: (a) the term "national security" is distinct from the term "national interest" or "public interest"; and (b) the powers under the proposed regime will not be exercised for the purposes of industrial policy, short term political expediency, other political or economic reasons (such as safe-guarding jobs in the UK) or in a manner which would undermine the legitimate benefits of foreign investment in the UK. Alternatively, the examples of trigger event risk that are set out in the SPI – *i.e.*, the potential for disruptive or destructive actions, espionage or inappropriate leverage – could be put on statutory footing in the Bill as situations in which a national security risk would occur.

2.4 In addition, the Bill should make clear that the call-in power will only be exercised in circumstances where <u>all three risk factors</u> (target risk, trigger event risk and acquirer risk) are present.

3. SCOPE OF REGIME

<u>Mandatory notification regime</u>

3.1 The Committee believes that the currently proposed mandatory notification regime does not meet a cost/benefit analysis and is disproportionate in view of the dangers of a small number of transactions against which it is trying to protect. Among other reasons, this is due to the breadth of the 17 sectors set out in the proposed secondary legislation, and, as is mentioned elsewhere, the breadth of the proposed regime's extra-territorial scope, the absence of a *de minimis*, the absence of clear safe harbours, the fact that transactions which close without approval will be void and that criminal sanctions will apply.

3.2 Specifically, the 17 sectors set out in the Secondary Legislation Consultation are very broad in scope and some of the sectors (for example, artificial intelligence or communications) could potentially capture almost any business in one way or another. As noted below, in the Committee's view the proposed mandatory regime may in particular cause serious damage to the UK as a hub for the technology sector (both as regards the establishment of businesses and their development and growth through continued investment).

3.3 As currently proposed, the breadth of the mandatory regime and the very serious potential consequences of failing to make a notification will force investors to take an over-cautious approach on many acquisitions

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[1] Such as, for instance, threatened intervention on the basis of disagreement with the acquirer's business model and/or investment strategy in relation to the acquisition of GKN by Melrose in 2018.

[2] For example, Australia's foreign investment regime defines national security as "*defence, security, international relations or law enforcement interests*", with "*international relations*" meaning "*political, military and economic relations with foreign persons and international organisations*".

and investments (including potentially essentially passive minority investments) and either seek informal guidance or make a voluntary notification even if they do not think a mandatory notification is required. This is likely to mean that the volume of enquiries/notifications is far higher than currently anticipated. When viewed in the context of the relatively small number of cases that are expected to be called in, this highlights the lack of proportionality of the proposed regime.

3.4 The Government has noted in its response to the National Security and Investment White Paper (the ***Response***) that certain other countries have recently introduced or broadened mandatory notification requirements in their foreign investment laws. However, those countries are in a different position to the UK. The UK is and seeks to be an open and international trading centre – adverse impacts on foreign investment would severely disrupt one of the key underpinnings of our economy. In addition, while countries such as the US have mandatory notification regimes, they generally apply in much more limited circumstances than is proposed with the 17 sectors set out in the Secondary Legislation Consultation.

3.5 Therefore, in the Committee's view the breadth of some of the 17 sectors (as currently proposed in the draft secondary legislation) should be significantly narrowed. The Committee intends to provide specific comments in due course on the Secondary Legislation Consultation, but would note in particular that the artificial intelligence sector, and the communications sector, would each potentially capture an overly wide range of businesses and could potentially cover almost any sort of business.

<u>Void transactions – mandatory regime</u>

3.6 The Committee believes it is unworkable to render a transaction automatically "void" – in other words of no effect such that the parties are regarded as being put back in the position they would have been in had the deal not happened – if it does not comply with the mandatory notification regime. Given the breadth of the regime, any such failure to notify could be wholly inadvertent. The Committee notes that the two longest standing foreign investment regimes – CFIUS in the US and FIRB in Australia – do not have this concept. The proposed approach is also inconsistent with the ability provided for in the Bill for a party to notify a retrospective validation application. If the original transaction was automatically void then it could not be ratified. As noted below, we believe any such transactions should be "voidable", not "void".

3.7 The use of the concept (of "voidness") will not promote clarity and predictability – there are in particular a very large number of uncertainties and potentially unintended consequences associated with rendering a transaction void. For example, if the relevant transaction had to be unwound and the relevant business returned to the seller, it is very unclear who would bear losses and liabilities in the relevant business which had occurred in the meantime. It is equally unclear how underlying financing and security arrangements would be impacted, how proceeds which have been distributed to selling shareholders would be recovered, and how to deal with any intervening on-sale or licensing of acquired assets.

3.8 The Committee also notes that rendering a transaction "void" could have significant adverse consequences for the seller, who may be forced to take back a business which it has not owned for some time and cannot then re-acquire, and other innocent third parties (with no direct connection with the transaction or the relevant national security risk). There is also the potential for very significant disruption to the business in question which may have adverse consequences in relation to the relevant "sensitive" sector in which it operates. If the buyer is the "bad actor" then it should bear the consequences, not the seller or other third parties. The prospect of rendering a transaction "void" would undermine clarity and predictability and may also cause transacting parties to seek to avoid the use of English law in transaction documents, which could give rise to international conflicts of law issues and would be detrimental to London's status as a leading financial and legal centre.

3.9 The concerns mentioned above are particularly acute in the context of public market transactions involving listed companies such as transactions subject to the Takeover Code and other public market transactions such as placings and rights issues. It would, in particular, seem exceptionally difficult, and particularly unfair, to seek to claw back money and property from public market investors including innocent retail investors who have had no direct involvement in the transaction. In addition, in relation to capital markets transactions such as placings and rights issues, the Committee is also concerned that regulated entities may be dissuaded from committing to underwriting arrangements in circumstances where a mandatory notification trigger event might be crystallised and therefore the transaction nullified.

3.10 The Committee believes that typical merger control remedies that are used under the EA 2002 regime should be sufficient and proportionate to address any national security concerns – for example, interim orders can be used to prohibit or reverse any aspect of integration between the buyer and the target and, in serious cases, divestment by the buyer to a third party could be required.

3.11 If the Government is in any event minded to have a regime which contemplates that transactions may be unwound in some cases (which, in the Committee's view, is disproportionate), then clause 13 of the Bill should instead provide that relevant transactions are "voidable", not "void" – in other words, the transaction would be regarded as effective unless and until the Secretary of State determines otherwise. In addition, the proposed regime should expressly provide (perhaps in the SPI) that interim orders and a forced divestment are expected to be sufficient in almost all circumstances and that unwinding a transaction would be a last resort only in exceptional circumstances where other remedies were not possible or not sufficient. In addition, as noted above, the fact that the Secretary of State has the power under the Bill to validate retrospectively a void transaction is inconsistent with a regime that purports to make transactions void, but would be much more consistent with a regime under which transactions might be voidable.

3.12 In addition, if the Government is ultimately minded to continue to have the Bill provide for transactions to be "void" (despite the concerns expressed in this paper), or the ability to avoid transactions in certain circumstances, consistent with the Law Society's Parliamentary Briefing dated 24th November 2020 the Committee believes transactions subject to the Takeover Code and certain other public market transactions (such as underwriting arrangement for placings and rights issues) should be exempted (or granted a safe harbour) from these consequences for the reasons mentioned above. The Government could always retain its rights to use the typical merger control remedies referred to in paragraph 3.10 in respect of these transactions.

Foreign/UK nexus

3.13 The extra-territorial jurisdiction of the proposed regime is significantly overbroad and disproportionate. Clause 8 of the Bill brings a very wide range of foreign transactions, businesses and assets within the scope of the proposed regime[3]. The Government's ability to take effective enforcement action in respect of transactions where there is no tangible UK nexus is in any event questionable.

3.14 To give one example, the definition of a qualifying asset in clause 7(6) of the Bill appears to catch assets that are used by one party in connection with sales to the UK that are made by an unrelated third party. If so, that would mean that investors in an extremely broad range of overseas businesses and/or assets would have to perform extensive due diligence to determine whether the assets are used in connection with goods or services which are ultimately supplied to persons in the UK.

3.15 The currently proposed extra-territorial jurisdiction of the proposed regime would also make it an outlier when compared with foreign investment regimes in other countries. For example, none of the foreign investment regimes in Australia, Canada, France, Germany, Spain or the United States assert jurisdiction over acquisitions of foreign businesses just on the basis of supplying goods or services to the relevant jurisdiction or ownership of assets that are used in connection with supplying goods or services to that jurisdiction. In addition, this may also have other adverse consequences: first, it may unnecessarily increase the filing burden on the new Investment Security Unit, for little benefit; and second, it may encourage other countries to take a similar approach and change their foreign investment regimes so that they can also intervene in foreign transactions (in places such as the UK), to the detriment of UK businesses and the UK market.

[3] Any supply at all into the UK would make an entity a qualifying entity – there is no need for the supply to have any connection with a potential target risk. In addition, assets used "in connection with" supplies to the UK would include assets (such as intellectual property rights) that are used in connection with products or services supplied to the UK by third parties.

3.16 The proposed regime should therefore apply only to the acquisition of UK entities or assets located in the UK. Specific concerns relating to off-shore assets should be dealt with through other regulation.

Domestic acquirers

3.17 The proposed regime also applies to transactions by domestic acquirers. In the Committee's view, this is unnecessary and disproportionate, and would give rise to significant uncertainty for domestic transactions. Concerns relating to domestic investment and acquirers would be more appropriately dealt with under other regulation – for example, confiscation proceedings under the Proceeds of Crime Act 2002 or the director disqualification regime.

3.18 The Committee also notes that other foreign investment regimes (including, again, Australia and the United States) do not apply to domestic acquirers in this way.

De minimis threshold for small transactions

3.19 The Committee believes that there should be a *de minimis* threshold below which transactions would not be subject to the mandatory notification. If that were the case, the Government could still retain the ability to call in any relevant transaction (even if below the mandatory filing threshold) in circumstances where national security is deemed to be at risk.

3.20 In the Committee's view, it is counterintuitive that small businesses and assets, and businesses and assets to which the market attributes a low value, would be likely in the vast majority of cases to give rise to material national security concerns.

3.21 The Committee believes the absence of a *de minimis* threshold will again increase the likelihood that Government is inundated with notifications and requests for informal guidance in relation to transactions which are inherently very unlikely to pose any material risk. This burden (both for the Security Investment Unit and the parties involved in the transactions) seems entirely disproportionate given the likelihood of potential risk. The Committee notes that, earlier this year, the *de minimis* threshold was removed from the Australian foreign investment regime, with the consequence that FIRB was inundated with notifications and expectations on clearance times in the middle of the year inflated by at least several months.

3.22 The Committee is also particularly concerned that this could have a serious chilling effect on investment in the technology sector in the UK. In particular, the proposed regime may have a detrimental impact on seed and venture-type investments, as early-stage start-ups are unlikely to have the resources to devote to managing the complexities of the proposed regime and their investors may not be prepared to participate in early (or even later) funding rounds. See also the comments in paragraphs 5.1 and 5.2 with regard to "Customary minority investor rights". The Committee also notes that if the Investment Security Unit is inundated with notifications of benign transactions that will make it more difficult for it to identify and investigate those transactions that give rise to genuine national security concerns.

3.23 A financial threshold below which the mandatory notification regime would not apply should be introduced. If the Government disagrees with adopting a general financial threshold for the mandatory regime (for example, because it believes that would not be appropriate in some of the sectors), then sector-specific financial thresholds should be introduced in the secondary legislation.

15% trigger for mandatory notification regime is inappropriate

3.24 The 15% trigger for mandatory notification in clause 6(2)(b) of the Bill is disproportionate in concept and should be deleted. The 15% trigger will lead to a disproportionate number of costly filings. If that trigger were deleted, the voluntary notification regime (and the power to issue a call-in notice) would still catch scenarios in which material influence is conferred (under clause 8(8) of the Bill). It is unclear in any event to the Committee whether a filing in relation to this trigger would really provide the proposed regime with useful information. In addition, if this trigger is retained, it is unclear to the Committee why it should be triggered by the acquisition of non-voting shares. See also paragraphs 5.1, 5.2 and 5.25.

4. REVIEW PROCESS

General

4.1 In light of the very broad scope of the proposed regime, the mandatory filings regime and the potentially significant uncertainties as regards interpretation and application of the regime, the Committee is concerned that the Government has significantly underestimated the likely number of notifications (both mandatory and voluntary) and the demand for informal guidance. The Committee also notes that if the Investment Security Unit is inundated with notifications of benign transactions that will make it more difficult for it to identify and investigate those transactions that give rise to genuine national security concerns.

4.2 It is therefore vital that the new Investment Security Unit, which will sit within the Department for Business, Energy and Industrial Strategy (***BEIS***), is adequately staffed and has the necessary resources to manage significantly higher numbers of notifications than the Government is currently anticipating within the timelines contemplated by the Bill and to provide meaningful informal guidance on a timely basis.

4.3 It is also very important that the Investment Security Unit develops an effective regime of guidance in order to promote certainty and predictability. It will be important in relation to the standing of, and level of confidence in, the regime that applications are capable of being processed from the outset in line with the stated timings and in a manner which is efficient and predictable. The Committee believes that, as currently proposed, there is a significant danger that the Government will be overwhelmed by requests for guidance in respect of the proposed regime (in particular, at the beginning of the proposed regime)[4].

Written guidance

4.4 In this respect, the Committee welcomes the guidance given in the SPI. However, the Committee believes it is not currently sufficient to provide market participants and their advisers with enough clarity as to how the proposed regime will work in practice.

4.5 The Committee anticipates that an effective regime of guidance will require the Government to issue more detailed written guidance (over and above the current SPI). This guidance should apply as from the commencement of the proposed regime and be updated on a periodic basis as and when relevant. In addition the Committee does not believe a review of the SPI every five years will be sufficient. There should be an annual review[5] which includes information setting out aggregated information on filing volumes and outcomes broken down by home country of the acquirer and sector of activity of the target, where relevant the circumstances in which transactions were blocked and the types of undertakings sought, and other important matters which have arisen.

Due process

4.6 Given the quasi-judicial capacity in which the Secretary of State will make decisions, the Bill should set out the due process rights that will be afforded to investors, including rights to be made aware of the nature of the Government's concerns and to be able to respond effectively to those concerns. Alternatively, the Bill should include a requirement for the Secretary of State to issue procedural rules by way of a regulation, e.g. like the rules issued under section 51 of the Competition Act 1998.[6]

Consultative guidance

4.7 While the Bill sets out proposed timescales for the formal stages of any notified transaction, it will be just as important for parties to understand the timescales and process that will be involved in seeking effective

[4] The Committee also believes that the Government could consider managing this by introducing the 17 sectors that are subject to the mandatory regime in phases – for example, by having a smaller number of the most sensitive sectors subject to the new regime from its commencement and introducing further sectors as the review process becomes predictable and established.
[5] This would be a separate exercise to the annual report required by clause 61 of the Bill.
[6] The Competition Act 1998 (Competition and Markets Authority's Rules) Order 2014.

consultative guidance. Currently it is not apparent how quickly such guidance might be obtained and how definitive it will be.

4.8 In addition, the Committee believes that the Government will need to develop a system of effective consultative guidance in relation to: (a) transaction specific matters – see below; and (b) general acquirer risk without reference to a specific transaction – also see below.

Transaction specific matters

4.9 The Committee believes there will be potentially significant complexity in advisers providing effective advice and guidance in relation to the proposed regime in the context of certain transactions, which the consultative guidance system will need to be designed to address. The Government should also clarify that it intends to cooperate with any potential acquirer during any pre-notification phase, in particular as the review timetable can be halted where filings are deemed to be incomplete which may lead to concerns over the predictability of the timetable under the regime.

4.10 Although it is welcome that the Government is seeking to cater in the SPI for providing guidance in relation to auction processes, it is unclear when exactly this facility will be available and how it will work in practice. In particular, it is worth reiterating that there will potentially be a large number of parties involved in an auction process (for example, bidders, potential consortium members, potential finance providers, potential suppliers and the seller/sponsor), all of whom may seek informal up-front discussions with the Government.

Acquirer risk

4.11 The Committee welcomes the guidance in the SPI around state-owned entities, sovereign wealth funds, other entities affiliated with foreign states and pensions funds.

4.12 The Committee is however particularly concerned that some foreign investors who are much valued in supporting UK investment (for example, sovereign wealth funds, pension funds or other state-affiliated investors) will be reluctant to incur the time and expense of participating in competitive sales/investment processes for potentially in-scope UK assets where there is material uncertainty over whether, and if so how, the regime will apply. This is especially given the risk of being publicly identified as being scrutinised as a potential threat to national security. The Committee anticipates that these investors will want to seek informal, consultative guidance on their risk profile and that the Government should be prepared to give such effective informal guidance on a timely basis, even if on a non-binding basis.

4.13 The Government notes in the published materials that it does not intend to publish as a routine matter call-in decisions, and will only do so when it is appropriate (e.g., where there is price-sensitive information that needs to be disclosed to the market). The Government has also stated that it will publish information following the assessment process in relation to cases resulting in final remedies (including blocking orders). While the Committee does not have significant objections to these proposals, the Committee believes that it should be made expressly clear under the proposed regime that an investor will be able to withdraw its notification and abandon its transaction during a short period after it is called in so as to avoid any potential reputational inferences.

4.14 The Committee also notes that nationality-based exemptions (through trade agreements) are for instance available in the CFIUS regime in the US, and suggests that the Government considers including some sort of "pre-approved" concept of acquirer in the proposed regime – whether by reference to jurisdiction, type of organisation (e.g., a regulated bank), pre-existing record as a long-established investor in the UK, or certain characteristics (e.g., a retail investment fund or non-state controlled entity). The Committee does not consider that the proposed power in clause 6(5) of the Bill is sufficient in this respect, as such exemptions should be from the scope of both the voluntary and mandatory filing regimes, which would require an additional power for the Secretary of State to exempt certain transactions from the definition of a trigger event. The Committee also recommends that a fast-track process is introduced (similar to the French regime in respect of listed companies) to avoid undue delays in more straightforward cases.

4.15 In addition, the Committee also notes that the requirement in the draft notification form to disclose "the aggregate percentage of any beneficial ownership by nationality" with no de minimis threshold is a huge task in practice for many entities and will not be possible in all cases.

Conditional transactions

4.16 Although it is unclear, the Committee understands that the obligation to notify (in the mandatory notification regime) and the ability to notify (in the voluntary notification regime) in the context of a conditional transaction would only arise at a time when it is likely that the conditions will be satisfied.

4.17 In the context of many conditional transactions, that may be too late for the transaction parties, who would typically want as much certainty as practicable before the conditional agreement is signed. At a minimum, the Investment Security Unit should be prepared to give meaningful and prompt guidance at an early stage. In addition, the Committee notes that it is possible to make a formal filing under many competition regimes upon signing of a transaction (even if conditional) and believes that it should also be possible under the proposed regime.

5. SPECIFIC AND DEFINITIONAL ISSUES

Customary minority investor rights

5.1 Under clause 8(6) of the Bill, one of the trigger events is acquiring "*voting rights that enable the person to secure or prevent the passage of any class of resolution governing the affairs of the entity*". The scope of this trigger event is unclear (in particular, precisely what resolutions "govern the affairs of the entity"), and in addition could potentially capture basic minority investor protections which would not give rise to national security concerns. In addition, other triggers for mandatory notification or the application of the voluntary regime are likely to largely 'overlap' with this trigger event – i.e. 15%, 25%, and material influence. In the Committee's view, the Government should consider removing this trigger event and if it is not minded to do so, to consider amending the trigger event so that it applies only in respect of all or substantially all of the matters which could be passed by ordinary or special resolution of a company incorporated under the Companies Act 2006 or in respect of veto rights in respect of all or substantially all of those matters (i.e where the veto rights go beyond customary minority protections – see paragraph 5.2 for more on minority protections).

5.2 In addition to the above, to promote certainty the Committee also recommends that a specific safe harbour is introduced for investors which have customary structural minority rights – for example, where a minority investor has consent or veto rights in relation to changes to constitutional documents, customary anti-dilution protections and other customary structural minority protection rights. This would be consistent with the regime applicable to people with significant control over a company under the Companies Act 2006 (***PSC regime***), where the statutory guidance includes examples of minority protection rights that would not be considered as conferring significant influence or control for those purposes.

Passive investors in funds

5.3 Passive investment (in particular in the form of limited partnership interests) is crucial to the functioning of the investment industry generally. The treatment of limited partners under the proposed regime will be critical to maintaining the attractiveness of the UK as a destination for foreign investment in investment funds.

5.4 The Committee believes that limited partners of a limited partnership (wherever formed), as passive investors without the right to exercise material influence over underlying investments, should be granted a safe harbour similar to the safe harbour contained in the PSC regime. Any such safe harbour should make clear that the participation by a limited partner in an advisory committee with the general partner or similar body would not remove the safe harbour, provided that the committee does not have the ability to control investment decisions.

Loan arrangements

5.5 London is a leading market for international finance, especially syndicated lending and the related secondary loan market. The treatment of loans under the proposed regime, absent appropriate safe harbours, could potentially have a seriously detrimental effect on the London finance market and its position in the global financial marketplace. This applies equally to debt securities and derivatives, for which there should be a complete exclusion.

5.6 In the SPI, it is stated that although loans are not exempt from scrutiny the overwhelming majority are expected to pose no threat to national security. In the Committee's view, it is unclear in what circumstances (absent appropriation of security) loans could be subject to the proposed regime. This sentence in the SPI arguably creates more uncertainty than it resolves, as it is unclear under what circumstances the Government is envisaging that lending might be problematic.

5.7 The standard Loan Market Association (***LMA***) loan facility (either bilateral or syndicated) will contain market standard information provisions and other covenants which would not give the lenders the ability to materially influence the strategy or management of the borrowing entity or the ability to use a qualifying asset which would give rise to national security concerns. The Committee believes that loan agreements documented on LMA standard terms or substantially similar terms should therefore be exempted from the proposed regime in order to promote certainty and predictability.

5.8 The Committee also believes that specific safe harbours in the proposed regime should be created for: (a) syndicated loans entered into by a syndicate of lenders substantially on LMA terms; (b) security held by a security trustee, where no single lender can direct the security trustee to enforce; and (c) bilateral loans by any bank regulated by the PRA, FCA or any third country authority recognised as equivalent by the Bank of England/Treasury.

5.9 In addition, lenders will likely want certainty before entering into a loan that there will not be impediments under the proposed regime if they need to enforce security. At present, there seems to be no mechanism in the Bill that would allow for that, as enforcement of security would not be reasonably in contemplation at the point in time when the loan is made. See the recommendations made in paragraph 4.17.

Land

5.10 In the absence of any register of sensitive land or some other means of checking whether land is sensitive, it would not be possible to predict whether or not a real estate transaction would be subject to the proposed regime, irrespective of the target's business. This would in fact be unworkable, as there would be no means at all of knowing whether or not a trigger event might occur. Therefore, a (i) register of sensitive land, for instance including at a minimum where known facilities are located; and/or (ii) database or facility in which a potential acquirer could check whether any land is or might be sensitive (e.g., by searching for a postcode), should be created. The Committee appreciates that a publicly accessible register of all sensitive land would not be desirable from a national security perspective. However, it believes that a combination of the above suggestions may make the application of the proposed regime workable in relation to land.

Licenses of intellectual property

5.11 In the Committee's view, the scope of intellectual property transactions that would be caught is unduly broad in a number of ways. In general, the proposed regime should (in order to be proportionate to the threat and manageable) be targeted at the transfers of control of intellectual property that is the specific focus of the Government's national security concerns in this area.

5.12 The mere licensing of intellectual property rights should not, on its own (i.e., without an associated transfer of control of the underlying subject matter of the intellectual property right), give rise to a national security concern. Subjecting the licensing of intellectual property to the proposed regime could lead to an insurmountably large number of concerns and notifications relating to such licensing arrangements, very few of which are likely to lead to any national security concerns and could severely undermine the UK technology sector.

Indirect holdings

5.13 Paragraph 3 of Schedule 1 to the Bill provides that a person holds a right or interest indirectly if the person has a majority stake in an entity and that entity: (a) holds the interest or right; or (b) is part of a chain of entities each of which (other than the last) has a majority stake in the entity immediately below it in the chain and the last of which holds the right or interest[7].

5.14 The Committee notes that this provision is consistent with an equivalent provision in the Companies Act 2006 governing indirect holdings in respect of the PSC regime. The Committee suggests that the explanatory note referred to in footnote 7 is amended so that it is clear that the person at the top of the chain (where there are more than two entities in a chain) must have a majority stake in the entity immediately below it in order for paragraph 3 of Schedule 1 to the Bill to apply. This is what the Bill provides for but the explanatory note is potentially ambiguous. It should also be made clear that not all "controlled" entities in the chain need to make separate applications under the regime in order to avoid the need to make multiple applications in relation to a single transaction.

5.15 The Committee also assumes that, as is the case with the concept of significant influence or control in the PSC regime, the material influence concept in clause 8(8) of the Bill is only intended to capture direct material influence (and, therefore, paragraph 3 of Schedule 1 to the Bill is not relevant when considering whether or not a person has material influence over an entity). The Committee suggests that this point is also clarified, as paragraph 3 of Schedule 1 to the Bill is expressed to apply to an “interest or right”, which could be ambiguous in this context.

5.16 See also paragraph 5.26 regarding excluding voting rights held by the entity itself when applying the indirect holdings test.

Intra-group transactions

5.17 Clause 10(2)(b) of the Bill appears to catch intra-group transactions, such as where an ultimate parent company holds an interest indirectly through a wholly-owned subsidiary and decides to transfer the interest to itself so that it is held directly. Such transactions do not raise new or additional national risks as there is no change in the substance of control and, for mandatory filings, the initial acquisition will already have been notified and reviewed. In addition, it would be disproportionate to create potential criminal liabilities for multinational companies that fail to identify a mandatory filing requirement arising from a purely intra-group restructuring in another jurisdiction.

Common purpose

5.18 Paragraph 11 of Schedule 1 to the Bill is extremely broad and could trigger mandatory filing obligations (and the associated criminal liability and the potential for the transaction in question to be void) if two investors do not accurately assess whether they share a “common purpose”, for which there is no definition and only the non-exhaustive example of co-ordinating their influence on activities, operations, governance or strategy.

5.19 While it is understandable that the Government wants to include such a provision to avoid circumvention, it will in the Committee’s view create a lot of difficulties for genuine/non-hostile investors if there is not a clearer statutory test as to what amounts to a common purpose. For example, do all investors in a consortium that is seeking to acquire an asset have a common purpose? What about investors which typically vote together/invest together but without a formal agreement or arrangement in this regard? The Committee recommends that a clear definition of “common purpose” is included in the Bill.

[7] The explanatory notes to the Bill (at p. 17) explain this as follows: “*This means that a person holding an interest or right in a parent entity of an entity or a chain of entities is, depending on the circumstances in sub-paragraph (2)(a) or (2)(b) being satisfied, treated as holding the interest or right in the entity at the bottom of the chain. If an entity is part of a chain of entities, a person will exercise the right indirectly if each entity in the chain has a majority stake in the entity immediately below it in the chain, and the last entity in the chain has the right in question.*”

Call-in power

5.20 The Government may issue a call-in notice at any time before the earlier of: (a) six months after the Secretary of State became aware of the trigger event; and (b) five years after the trigger event. There is no clear provision on when the Secretary of State might become aware of a trigger event for these purposes. In order to given investors certainty, as with the competition regime, there should to be a clear provision in the Bill (and related guidance) specifying when the Secretary of State will be deemed to have become aware of a trigger event for these purposes. In particular, the Secretary of State should be deemed to have become aware of a trigger event if it is notified to BEIS or if it is made public (and the EA 2002 contains a definition of "made public" for these purposes).

Impossibility

5.21 Clause 6(3) of the Bill creates a potential loophole that could be exploited if a foreign government were to prohibit its domestic investors from notifying or providing information that is necessary to make a mandatory notification. The Committee recommends that wording is added to the clause to clarify that conflicting obligations under the law of a foreign jurisdiction will not suffice to establish the impossibility of compliance.

Carrying on activities / business

5.22 There is a mis-match between the wording that is used to define an extra-territorial "qualifying entity" for the purposes of clause 7(3) of the Bill ("carries on activities in the United Kingdom") and the scope of extra-territorial conduct that may be subject to a final order under clause 26(6) of the Bill ("carrying on business in the United Kingdom"). The Committee recommends aligning these provisions by using the concept of "carrying on business" in clause 7(3), as that concept is also used under the EA 2002 and was considered by the Court of Appeal in the Akzo / Metlac judgment.[8]

Interaction with the Takeover Code

5.23 It is noted that the published materials provide that the Government will work closely with the Takeover Panel to ensure that the proposed regime interacts efficiently and effectively with the Takeover Code.

5.24 The Committee notes that the Takeover Panel is currently consulting on certain amendments to the Takeover Code, including proposed amendments to remove the current favourable treatment for UK/EU merger clearance conditions. The Committee believes that the Takeover Panel and the Government should clarify the circumstances in which a bidder may seek to invoke a condition relating to approval under the proposed regime as soon as possible.

Determining percentage of shares and voting rights

5.25 For the purposes of clauses 6(2)(b) and 8(2) of the Bill, acquisitions of non-voting shares count towards the relevant thresholds. It is not clear how the acquisition of non-voting shares could give rise to effective control or national security concerns and the Committee recommends that the Government considers excluding non-voting shares from the calculation of the relevant thresholds in the Bill.

5.26 The Government should also consider whether voting rights held by the entity itself should not count towards the relevant thresholds in respect of voting rights in clause 8(5) of the Bill and when applying the indirect holdings test in paragraph 3 of Schedule 1 of the Bill. Such shares are excluded from the second condition (i.e. holding more than 25% of the voting rights in a company) of the PSC regime and when applying the "indirect" test in the PSC regime (see paragraph 15 of Schedule 1A of the Companies Act 2006).

5.27 Clause 8(3)(b) provides that when determining whether a person has increased their percentage of "shares" through one of the relevant thresholds in respect of an entity that does not have a share capital, "percentage of shares" refers to holding a right to a share of that percentage of the capital or profits of the entity. For

[8] *Akzo Nobel N.V. v Competition Commission & Ors* [2014] EWCA Civ 482 judgment of 14 April 2014.

some entities (e.g. limited partnerships) this percentage may be difficult to determine because profit sharing arrangements can be varied and complex. Such arrangements may also mean that a person's percentage share of the profits fluctuates over time and throughout the year. The Government should consider whether "percentage of shares" for an entity that does not have a share capital should refer to a right to a share of that percentage of any surplus assets of the entity on a winding up, as is the case for LLPs in clause 8(3)(c) of the Bill. Condition 1 of the PSC regime for LLPs and Scottish limited partnerships refers to holding the right to more than 25% of any surplus assets on a winding up.

Transitional regime

5.28 The retrospective application of the legislation, as set out in the Bill, is stated as being designed to ensure that transactions that might otherwise be caught under the proposed regime are not implemented on an accelerated timeline to escape the remit of the proposed regime.

5.29 This presents particular uncertainty in respect of transactions which signed before 12th November 2020, as well as transactions signed after 12th November 2020 but before commencement of the Bill. In particular, transactions signed before 12th November may not have accounted for this deal risk through appropriate conditionality. In addition, transactions which do not close before the commencement date of the Bill may be subject to a mandatory notification obligation after the commencement date. This could delay closing even for innocuous transactions (including investments in foreign entities).

5.30 Given the stated purpose of the retrospective application of the legislation (as noted above), transactions signed before 12th November 2020 should be exempt from the operation of the Bill, as it is unlikely that the relevant parties can be said to have accelerated a transaction to fall outside of the proposed regime given they would not have known when it might be introduced or on what terms. In addition, given the difficulties and complexities of the proposed retrospective operation of the Bill, the Committee also considers that a formal exemption should be introduced for transactions signed after 12th November 2020 but before commencement of the Bill if they are pre-vetted by BEIS.

5.31 As a practical matter, many acquirers to whom the retrospective application might apply will presumably decide to seek guidance from BEIS, not least because this limits the period in which, after the commencement date, a call-in notice might be issued. The Committee assumes that BEIS is both staffed appropriately to deal with this and will be in a position to give clear, effective and timely guidance to mitigate potential transaction risks.

5.32 Clause 62 of the Bill states that the relevant parts of the EA 2002 regime may still apply during the transitional period. This simultaneous application of both the EA 2002 and the Bill will compound investors' uncertainty as to the retrospective application of the proposed regime. The Committee recommends that the practical interaction, during the transitional period, of the EA 2002 regime and the proposed regime is clarified.

ANNEX

1. The views set out in this paper have been prepared by a Joint Working Party of the Company Law Committees of the City of London Law Society (***CLLS***) and the Law Society of England and Wales (the ***Law Society***).

2. The CLLS represents approximately 17,000 City lawyers through individual and corporate membership, including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multijurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

3. The Law Society is the professional body for solicitors in England and Wales, representing over 170,000 registered legal practitioners. It represents the profession to Parliament, Government and regulatory bodies in both the domestic and European arena and has a public interest in the reform of the law.

4. The Joint Working Party is made up of senior and specialist corporate lawyers from both the CLLS and the Law Society who have a particular focus on issues relating to mergers and acquisitions and inbound investment.