

# UK MERGER CONTROL: GREATER SCOPE FOR GOVERNMENT INTERVENTION

25 June 2020

The UK government recently made and proposed revisions to the UK merger control regime, which are intended to increase its ability to intervene in transactions and investments (including foreign direct investment ("**FDI**")) affecting certain aspects of the UK economy.

While the UK does not currently have a specific legislative regime addressing FDI, the UK government has made clear its intention to introduce such a regime, with the National Security and Investment Bill announced in December 2019, and expected to be brought before Parliament later this year.

Pending the introduction of an FDI regime, the UK government's revisions to the UK merger control regime have been positioned as a form of "short term" risk mitigation,<sup>[1]</sup> and businesses should therefore expect further significant changes in relation to FDI in the UK in the coming months.

Against this background, this update considers the relevant revisions, and their implications for businesses.

## Enacted revision: Public health emergencies - the addition of a new "public interest" criterion

The Enterprise Act 2002 (Specification of Additional Section 58 Consideration) Order 2020 introduces a further "public interest" criterion to the UK merger control regime, in addition to the "public interest" criteria addressing (i) national security; (ii) media plurality; and (iii) the stability of the UK financial system.<sup>[2]</sup>

Under this additional public interest criterion, the UK government is able to intervene<sup>[3]</sup> where it believes that a transaction:

- may satisfy the general jurisdictional thresholds under the UK merger control regime;<sup>[4]</sup> and
- gives rise to considerations regarding the need to maintain in the UK the capability to combat, and to mitigate the effects of, public health emergencies (the "**Public Health Emergencies Criterion**").

Significantly, for the purposes of the UK merger control regime, the acquisition of a minority stake in a target company<sup>[5]</sup> (e.g. by a foreign investor) could be capable of review.

If the UK government is minded to intervene, the Secretary of State ("**SoS**") will issue a public interest intervention notice ("**PIIN**"), and the UK Competition and Markets Authority (the "**CMA**") will prepare a report for the SoS addressing jurisdictional and competition issues.

The CMA is usually the decision-maker when investigating a transaction under the UK merger control regime on competition grounds. However, where the SoS issues a PIIN, the SoS replaces the CMA as the decision-maker, meaning that it is for the SoS to determine whether the transaction is to be:

- cleared at the end of a Phase 1 investigation (with the parties potentially providing undertakings to address concerns in order to secure clearance); or
- referred for a Phase 2 investigation, having regard to public interest concerns in addition to any competition concerns.

If a transaction is referred for a Phase 2 investigation, the SoS will ultimately decide whether the transaction is in the public interest,<sup>[6]</sup> and if not, what remedy is required to resolve concerns identified at the conclusion of the Phase 2 investigation, including public interest concerns.<sup>[7]</sup> A remedy in this context could include the SoS prohibiting the transaction (in whole or in part).

## **Broad application of the Public Health Emergencies Criterion**

The Public Health Emergencies Criterion is widely drafted, and the accompanying Explanatory Memorandum<sup>[8]</sup> makes clear that its application is intended to go beyond any

direct public health response to a pandemic.

For example, in addition to noting that the UK government may need to intervene where a vaccine research company or a manufacturer of personal protective equipment is being acquired, the Explanatory Memorandum gives examples of such intervention potentially being required where the acquisition target is an internet service provider or food supply chain company, given "the potential for increased demand for internet services in a lockdown or disruption to food supply".

Moreover, the Public Health Emergencies Criterion is not limited to the current COVID-19 pandemic, with the Explanatory Memorandum confirming that the UK government must be able to intervene in advance of public health emergencies to ensure that "critical capabilities are not degraded before an emergency strikes".

Formal guidance is due to be published in relation to the Public Health Emergencies Criterion, and it would be helpful for this to confirm the intended parameters of its application, so as to provide businesses with a greater degree of clarity.

## **Proposed revisions: artificial intelligence, cryptographic authentication technology, and advanced materials**

By way of background to these proposed revisions, in June 2018 the UK government enacted specific lower jurisdictional thresholds under the UK merger control for transactions where the acquisition target (the "**Relevant Enterprise**") was involved in certain activities in connection with:

- the design and maintenance of aspects of computing hardware;
- the development and production of quantum technology; and/or
- the development or production of items for military or dual-use, including holding information capable of use in connection with the development or production of such items.

These lower jurisdictional thresholds are that:

- the annual UK turnover of the Relevant Enterprise exceeds £1 million; **or**
- pre-transaction, the Relevant Enterprise supplied or procured goods or services of a particular description, and had a share of supply or procurement of at least 25% of all of those goods or services in the UK, or in a substantial part of the UK.<sup>[9]</sup>

Where it is or may be the case that a transaction satisfies these lower jurisdictional thresholds, the CMA is able to investigate on competition grounds, and the SoS is able to intervene where it considers that the transaction may raise public interest considerations in relation to national security. Importantly, as noted above, if the SoS intervenes (i.e. by issuing a PIIN), the SoS then replaces the CMA as the decision-maker in relation to the transaction.

## Broad application of the proposed revisions

Under the UK government's proposed revisions, the sectors relevant to the activities of a Relevant Enterprise would be expanded, so as to include a range of activities in connection with the following broadly defined sectors of the UK economy:

- artificial intelligence ("**AI**");<sup>[10]</sup>
- cryptographic authentication technology;<sup>[11]</sup> and
- advanced materials.<sup>[12]</sup>

Significantly, the apparent intention is for these lower thresholds to have a broad application in the context of these three sectors.

For example, under the proposed revisions, the activities of a Relevant Enterprise would include:

- developing or producing anything designed for use in AI;
- supplying services employing AI, or cryptographic authentication technologies;
- owning, creating or supplying intellectual property relating to the functional capability of advanced materials;
- developing or producing anything designed as an "enabler", where this is not an advanced material, but is used in the manufacture of an advanced material; and
- providing know-how about enablers, or their use.<sup>[13]</sup>

Therefore, if enacted, the proposed revisions would afford the UK government far greater scope to intervene on national security grounds in relation to transactions affecting the AI, cryptographic authentication technology, and advanced materials sectors in the UK. The proposed revisions are not however anticipated to result in a material change to the CMA's approach to assessing such transactions on competition grounds.

These proposed revisions will now be debated by both Houses of Parliament, and require approval before they can enter into force.

# Implications for businesses

Against the backdrop of the National Security and Investment Bill and the UK government's clear intention to introduce a specific FDI regime, significant implications for businesses arise from both the Public Health Emergencies Criterion and the proposed revisions affecting the AI, cryptographic authentication technology, and advanced materials sectors.

In the first instance, businesses will need to consider carefully if and how the actual and proposed revisions may apply to their transactions, particularly if they are currently contemplating transactions that could be affected if the proposed revisions enter into force in the short term.

In addition, while the relevant enacted and draft legislative instruments do not distinguish between UK and non-UK entities, the accompanying Explanatory Memoranda expressly outline concerns that the financial uncertainty caused by the COVID-19 pandemic:

- could result in "UK enterprises with critical capabilities [being] more vulnerable to takeover";<sup>[14]</sup> and
- has increased "the risk of hostile actors exploiting the situation through aggressive acquisitions of UK businesses", as well as "the threat of the UK losing capability to act as a sovereign nation with its own capabilities".<sup>[15]</sup>

These stated concerns suggest that transactions involving certain non-UK entities can be expected to be subject to closer scrutiny by the UK government on public interest grounds, including national security.

Therefore, in addition to considering potential competition law concerns in the context of the UK merger control regime, businesses planning transactions that potentially fall within the scope of the relevant revisions should ensure that they engage at an early stage with the possibility of the UK government intervening, and the SoS assuming the role of decision-maker.

This engagement is likely to include commencing an informal dialogue with the relevant government department, as well as giving careful consideration to potential remedies that could be offered to address any concerns identified at a later date (including in relation to the possible re-structuring of the transaction). The risk of intervention by the UK government should also be addressed as necessary with the relevant transaction documents (e.g. in the context of a condition precedent), and the transaction timetable.

Businesses should also have in mind the UK government's positioning in relation to FDI,

and expect further developments in this regard.

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[1] See, "New protections for UK businesses key to national security and fight against coronavirus", BEIS press release, 21 June 2020.

[2] See, section 58 of the Enterprise Act 2002.

[3] See, section 42 of the Enterprise Act 2002.

[4] Whereby either (i) the annual UK turnover of the target enterprise exceeds £70 million; or (ii) the enterprises ceasing to be distinct both supply or procure goods or services of a particular description and, post-transaction, will supply or procure at least 25% of all of those goods or services in the UK, or in a substantial part of the UK.

[5] See, for example, RWE's anticipated acquisition of a 16.67% shareholding in E.ON, which was cleared by the CMA at Phase 1 (ME/6800/19 Anticipated acquisition by RWE AG of a 16.67% minority stake in E.On SE, CMA clearance decision of 5 April 2019); and Amazon's anticipated acquisition of a minority shareholding in Deliveroo (ME/6836/19 Anticipated acquisition by Amazon of a minority shareholding and certain rights in Deliveroo, CMA reference decision of 11 December 2019).

[6] See, section 54 of the Enterprise Act 2002.

[7] See, section 55 of the Enterprise Act 2002.

[8] Explanatory Memorandum to the Enterprise Act 2002 (Specification of Additional Section 58 Consideration) Order 2020, 2020 No. 627.

[9] The concept of a Relevant Enterprise, and the applicable lower jurisdictional thresholds, were introduced by The Enterprise Act 2002 (Share of Supply Test) (Amendment) Order 2018 (SI 2018/578), and The Enterprise Act 2002 (Turnover Test) (Amendment) Order 2018 (SI 2018/593).

[10] Defined within the proposed revisions as being "technology enabling the programming or training of a device or software to use or process external data (independent of any further input or programming) to carry out or undertake (with a view to achieving complex, specific tasks) (a) automated data analysis or automated decision making; or (b) analogous processing and use of data or information".

[11] Defined within the proposed revisions as being the method of verifying (a) the identity of a person, user, process or device; or (b) the origin or content of a message, data or information, by means of electronic communication, where the method of verification has been encrypted or subject to other analogous application.

[12] Defined within the proposed revisions as being "(a) any materials that are capable of modifying (including in real time) the appearance, detectability, traceability or identification of any object to a human or to sensors within the range 1.5e13 Hz up to and including ultraviolet; (b) any alloys that are formed by chemical or electrochemical reduction of feedstocks in the solid state; (c) any manufacturing processes that are involved in the

solid state formation of alloys in or into crude or semi-fabricated forms, or powders for additive manufacturing, where "additive manufacturing" means a process of joining materials to make parts from three-dimensional model data; or (d) any metamaterials that do not include (i) fibre-reinforced plastics in structural components, products or coatings with completely random dispersion of pigment or other filler; or (ii) any packaged device components that are designed for civil application".

[13] See, the draft statutory instrument, The Enterprise Act 2002 (Share of Supply) (Amendment) Order 2020.

[14] Explanatory Memorandum to the Enterprise Act 2002 (Specification of Additional Section 58 Consideration) Order 2020, 2020 No. 627.

[15] See, the draft Explanatory Memorandum to the Enterprise Act 2002 (Share of Supply) (Amendment) Order 2020.

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