

26 June 2020

# UK Merger Control

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## UK Government Adds to National Security Intervention Powers

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### SUMMARY

On 23 June 2020, the UK government added public health emergencies to the definition of “public interest” for the purposes of the Enterprise Act 2002. This permits the UK to intervene on public interest grounds in any transaction which meets the UK merger control regime’s thresholds and is connected with the UK’s “capability to combat, and to mitigate the effects of, public health emergencies”. This is more open-ended than first appears and could capture a broad array of transactions.

In addition, the UK government will shortly add artificial intelligence (“AI”), cryptographic authentication technology and advanced materials to the list of “relevant enterprises” first established in 2018, meaning that any transaction involving a target active in these areas in the UK will be subject to lower thresholds in applying the UK merger control regime and any public interest intervention, adding uncertainty to deals in these sectors.

There are also likely to be further changes to the UK government’s powers of intervention as it has said that it plans to shortly bring legislation before Parliament to implement a consultation carried out in 2018 on both extending the UK’s national security review regime and placing it on a new statutory footing.

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### I. COVID-19 AND PUBLIC HEALTH EMERGENCIES

#### A. BACKGROUND

The CMA is able to review a “**relevant merger situation**” for competition concerns under the Enterprise Act 2002 (the “**Enterprise Act**”). A relevant merger situation is defined generally as a transaction where two or more enterprises “cease to be distinct”, and either of the two thresholds below are met:

- The UK turnover of the target being acquired exceeds GBP 70 million (this threshold is lowered to GBP 1 million in certain sectors, as described in Part II of this memorandum); or
- The transaction creates or increases a combined share of supply of at least 25% of the sale or purchase of the relevant good or service in the UK or a substantial part of the UK (this threshold is different in certain sectors, as described in Part II of this memorandum).

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Where a relevant merger situation raises public interest considerations, the Secretary of State for Business, Energy and Industrial Strategy (the “**Secretary of State**”) can issue a “Public Interest Intervention Notice” (“**PIIN**”). A PIIN compels the CMA to begin an investigation of the transaction, and passes ultimate control of the CMA’s review to the Secretary of State, including the powers to block the transaction, or impose undertakings and remedies.<sup>1</sup>

Before 23 June 2020, the Secretary of State could issue a PIIN in relation to three defined areas of “public interest”: (i) national security, (ii) media plurality (an umbrella term covering a number of media-related considerations), and (iii) the stability of the UK financial system.

There have been 20 transactions where the UK government used a PIIN to intervene in a transaction since the Enterprise Act came into force: 12 on national security grounds; seven on media plurality grounds; and one on financial stability grounds. Since the start of 2019 there has been an increase in the issue of PIINs on national security grounds in particular. The UK government issued a PIIN to intervene in: (i) the acquisition of Cobham (a defence contractor) by Advent (a US private equity firm);<sup>2</sup> (ii) the acquisition of Mettis Aerospace by Aerostar (a Chinese investor);<sup>3</sup> (iii) the acquisition of Inmarsat plc (a satellite telecommunications company) by a consortium of non-UK private equity firms, including Apax Partners and Warburg Pincus;<sup>4</sup> and (iv) the acquisition of Impcross (a British engineering company) by Gardner Aerospace (a Chinese-owned aerospace company).<sup>5</sup>

### **B. NEW PUBLIC INTEREST CONSIDERATION**

The UK government has added the “*capability to combat, and to mitigate the effects of, public health emergencies*” to the list of public interest considerations in the Enterprise Act.<sup>6</sup> This means that, in any relevant merger situation where capability to combat public health emergencies is a “relevant” consideration, the Secretary of State can issue a PIIN and review the transaction under public interest grounds.

This new public interest consideration is quite broad, which is revealed in the explanatory memorandum accompanying the implementing legislation.<sup>7</sup> Although this memorandum is not legally binding, it gives important guidance as to the intention of the UK government in making the change. It does so by referring to a non-exhaustive list of examples of where the changed power might be used.

The first example is not unexpected: “*The Government may for example need to act if an enterprise involved in the fight against COVID-19, a vaccine research company or a manufacturer of personal protective equipment for instance, finds itself the target of a takeover.*”

However, a further example shows the potentially expansive nature of the change: “*the Government may for example need to intervene if an **internet service provider or food supply chain company** becomes the subject of a takeover, **given the potential for increased demand** for internet services in a lockdown situation or disruption to food supply.*” (Emphasis added).

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This is then broadened even further in another example: “*usually stable businesses may be suffering a short-term impact to their share price or profitability. This could leave UK enterprises with critical capabilities more vulnerable to takeover.*”

Therefore, it appears that the intention of the change would be to give the Secretary of State the power to intervene, on public interest grounds, in any transaction involving a target meeting the indicative thresholds that the UK government deems critical to the effort to “combat” or “mitigate” the effects of a “public health emergency” (a term that is not defined in the legislation). This gives potentially a very broad discretion to the UK government to intervene on public interest grounds in transactions in a wide variety of sectors, many of which would not previously have been thought to be susceptible to public interest intervention.

The Department of Business, Energy and Industrial Strategy will issue further detailed, non-statutory guidance in due course.

To date, no transaction has been prohibited on public interest grounds: the most frequent response following a PIIN is for the parties to offer undertakings to the Secretary of State (as was the case in Cobham, Inmarsat, and appears to be likely for Impcross). Parties have also abandoned transactions after receiving a PIIN (as was the case for Mettis Aerospace).

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## II. AI, CRYPTOGRAPHIC AUTHENTICATION TECHNOLOGY AND ADVANCED MATERIALS

### A. BACKGROUND

In June 2018, the UK Government added a new exception to the definition of a “relevant merger situation” (see above). Where a target meets the definition of a “relevant enterprise”, the thresholds for jurisdiction are lowered significantly. Instead of GBP 70 million of UK turnover, the target need only generate GBP 1 million of UK turnover. Alternatively, instead of requiring the *combined* entity to have a post-transaction share of supply of at least 25%, a relevant merger situation would arise if the “relevant enterprise” target *already* had a share of supply of at least 25%, regardless of whether that share of supply increases as a result of the transaction. Both thresholds are significantly easier to meet, expanding the CMA’s jurisdiction.

The definition of a relevant enterprise introduced in 2018 was a company active in any of the following sectors: (i) military or dual-use goods subject to export control; (ii) computer processing units; or (iii) quantum technology.

The significant lowering of the thresholds for relevant enterprises gave the potential, in relation to targets active in those sectors in the UK, for a relevant merger situation to arise in many more transactions than was previously the case. This also significantly increased the number of transactions in these sectors where the Secretary of State had the power to issue a PIIN.

## B. NEW RELEVANT ENTERPRISE SECTORS

The UK Government has tabled secondary legislation to add three new types of “relevant enterprise”, expanding the category of targets to which the lower thresholds apply.<sup>8</sup> Those new categories of “relevant enterprise” are those active in:

- Artificial Intelligence (including related research, services and development)
- Cryptographic Authentication Technology (electronic methods of verifying user identity and content origin)
- Advanced Materials and their inputs (defined as materials and alloys with specific physical properties)

The reason for adding these new “relevant enterprise” sectors now is that they were previously identified in a consultation run by the UK government in 2018, and have now been considered “*as parts of the economy where risks to national security were most likely to arise.*”<sup>9</sup>

By designating these sectors as “relevant enterprises”, transactions involving targets in those sectors that meet the much lower thresholds are now potentially reviewable under public interest grounds. This will add uncertainty to any transaction in these sectors.

## C. FURTHER NATIONAL SECURITY LEGISLATION ON THE HORIZON

In 2018 the UK government published detailed proposals for consultation for a new national security review regime, broader than the existing powers described above under the Enterprise Act.<sup>10</sup> The proposed regime would be broad in scope and would give the UK authorities extensive powers, and create a number of new criminal offences and civil penalties. It would also allow the UK government to review transactions giving rise to national security concerns, whether or not they were notified to the UK government voluntarily by the parties. Although the UK government said at the time that it expected the regime to focus on particular sectors, it also stated that the regime would apply to the entire UK economy, and overrule any determination made independently by the Competition and Markets Authority regarding the competitive effects of the transaction. The regime would also grant the power to scrutinise acquisitions of entities and assets that have not been caught by any previous UK regime, including acquisitions of land outside the UK, and acquisitions of data and intellectual property.

These proposals have remained dormant, and received some criticism when originally published.<sup>11</sup> However, in the press release announcing the amendments to the Enterprise Act described in this memorandum,<sup>12</sup> the UK government states that those amendments are being made “*in the short term ahead of more comprehensive powers in the forthcoming National Security and Investment (NS&I) Bill.*” It is clear that major developments to the UK government’s ability to intervene in transactions on national security grounds are on the horizon, and that these could involve the implementation of some or all of the 2018 proposals.

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ENDNOTES

- 1 The Secretary of State is nonetheless bound by the CMA's findings and decision in relation to the competitive effects of the transaction.
- 2 The UK government accepted undertakings from the acquirer. See <https://www.gov.uk/cma-cases/advent-international-cobham-merger-inquiry>
- 3 The transaction was ultimately abandoned. See <https://www.gov.uk/cma-cases/aerostar-mettis-merger-inquiry>
- 4 The UK government accepted undertakings from the acquirer. See <https://www.gov.uk/cma-cases/connect-bidco-inmarsat-merger-inquiry>
- 5 The investigation into this transaction is ongoing: the acquirer has submitted undertakings to the UK government. See <https://www.gov.uk/cma-cases/gardner-aerospace-holdings-limited-impcross-limited-merger-inquiry>
- 6 See Article 2 of The Enterprise Act 2002 (Specification of Additional Section 58 Consideration) Order 2020, available at <http://www.legislation.gov.uk/uksi/2020/627/contents/made>
- 7 See [http://www.legislation.gov.uk/uksi/2020/627/pdfs/uksiem\\_20200627\\_en.pdf](http://www.legislation.gov.uk/uksi/2020/627/pdfs/uksiem_20200627_en.pdf)
- 8 See <https://www.legislation.gov.uk/ukdsi/2020/9780348208795/contents>
- 9 See [https://www.legislation.gov.uk/ukdsi/2020/9780348208795/pdfs/ukdsiem\\_9780348208795\\_en.pdf](https://www.legislation.gov.uk/ukdsi/2020/9780348208795/pdfs/ukdsiem_9780348208795_en.pdf)
- 10 See <https://www.gov.uk/government/consultations/national-security-and-investment-proposed-reforms>
- 11 For example, see "Mergers and the public interest: a wolf in sheep's clothing?" by John Fingleton, available at <https://fingleton.com/wp-content/uploads/2018/10/John-Fingleton-Mergers-and-the-public-interest-a-wolf-in-sheeps-clothing-Oct-2018.pdf>
- 12 See <https://www.gov.uk/government/news/new-protections-for-uk-businesses-key-to-national-security-and-fight-against-coronavirus>

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## CONTACTS

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### London

Ben Perry	+44 207 959 8477	<a href="mailto:perryb@sullcrom.com">perryb@sullcrom.com</a>
Jeremy B. Kutner	+44 207 959 8484	<a href="mailto:kutnerj@sullcrom.com">kutnerj@sullcrom.com</a>
Vanessa K. Blackmore	+44 207 959 8480	<a href="mailto:blackmorev@sullcrom.com">blackmorev@sullcrom.com</a>
Juan Rodriguez	+44 207 959 8499	<a href="mailto:rodriguezja@sullcrom.com">rodriguezja@sullcrom.com</a>

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