



NATIONAL SECURITY AND INVESTMENT: MANDATORY NOTIFICATION SECTORS

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ICAEW welcomes the opportunity to comment on the consultation, *National Security and Investment: Mandatory Notification Sectors*, published by BEIS on 11 November 2020, a copy of which is available from this [link](#).

The Investment Security Unit (ISU) should disseminate information, by way of 'market guidance notes', on the assessment of businesses, assets and acquirers; for example, where it has identified trends; where further guidance would be useful on consulting the unit; and on the timing of an approach. This could also include commentary on emerging patterns or could set out the ISU's likely approach to certain situations. Market guidance notes can inform market participants, increase transparency and improve efficiency in the assessment process and in the operation of the ISU.

This response of 6 January 2021 has been prepared by the ICAEW Corporate Finance Faculty. Recognised internationally as a source of expertise on corporate finance issues and for its monthly *Corporate Financier* magazine, the faculty is responsible for ICAEW policy on corporate finance issues including submissions to consultations. The faculty's membership is drawn from professional services groups, advisory firms, companies, banks, brokers, private equity, law firms, consultants and academics.

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KEY POINTS

ICAEW and national security and investment policy

1. ICAEW has a keen interest in the objective of the new national security and investment policy and in the effectiveness of the scrutiny process. The proposed sector definitions are wide-ranging which, together with the absence of de minimis thresholds, are set to capture a significant number of transactions. The majority of these will likely be smaller transactions involving private companies and investors, not global businesses. These transactions will likely be advised by ICAEW members and/or its member firms; ie finance directors of business, investors, and the corporate finance businesses of professional services firms. Many such transactions will not hitherto have been subject to regulatory consultation, notification and assessment, and businesses, investors and advisers will face an asymmetry of information. Our principal point (see paragraph 3) envisages commentary and additional being routinely published.
2. This response forms part of ICAEW's ongoing consideration of and engagement regarding the new national security and investment regime. In November 2020, ICAEW participated in a roundtable meeting with the Minister for Business and Industry and the Minister for Investment on the National Security and Investment Bill. ICAEW's head of corporate finance, David Petrie, also gave evidence to the National Security & Investment Bill Public Bill Committee on 24 November 2020, as [reported in Hansard](#) and [broadcast on Parliament TV](#), and subsequently exchanged correspondence with the Minister for Business and Industry.

ISU should publish market guidance notes

3. We strongly believe that the Investment Security Unit (ISU) should publish guidance on matters that would benefit market participants. ICAEW also made this point to the Public Bill Committee. The ISU can disseminate information by way of 'market guidance notes' on the assessment of businesses, assets and acquirers; for example, where it has identified trends; where further guidance would be useful on consulting the unit and the timing of an approach. This could include commentary on emerging patterns or could set out the ISU's likely approach to certain situations. Market guidance notes can inform market participants, increase transparency and improve efficiency in the assessment process and in the operation of the ISU. Market guidance notes will be a flexible tool for the ISU to use to communicate its approach and expectations. Such a tool is used by regulators such as the FCA (Primary Market Bulletins) and the Takeover Panel (Practice Statements) and guidance issued by the ISU would be in addition to the planned annual report.

Other considerations applying to all mandatory notification sectors

4. We believe that specific guidance is needed urgently on the following matters:
 - the approach for deals completing before the Bill is enacted;
 - criteria for UK acquirers;
 - clarity on the scope of remedies – eg, is divestment to the seller envisaged?
 - help for businesses to self-assess (eg at company registration or formation of partnership) and to assess its assets and supply chains;
 - timing of notification in relation to the marketing of private transactions, and in relation to the timetable for public offers;
 - extent of responsibility for notification of businesses in undefined sectors.

QUESTIONS APPLYING TO ALL SECTORS

Question 1 *Are the sector definitions sufficiently clear to enable investors and businesses to self-assess whether they must notify and receive approval for relevant transactions? If not, how can the definitions be improved?*

Question 2 *To what extent are technical and scientific terms correct and sufficiently clear and commonly understood for the purposes of determining relevant activities?*

5. The principal driver to success of the regime will be businesses' awareness if they (the entities or their assets) are caught within the sectors. This will enable them to understand the implications of transacting with specific investors or acquirers. For some businesses, clear sector definitions may be straightforward to interpret. However, the range of sectors involved means that definitions will not be enough to help all businesses to self-assess. Many businesses will not be familiar with the existing, narrower national security regime or the Strategic Export Control lists. Others may be on the margins of the proposed sectors. Another group may not appreciate the proximity of their supply chain to defined sectors.
6. The government will, on an ongoing basis, need to:
 - educate businesses that they need to work out if they fall within a definition;
 - signpost and resource the ISU that businesses can pre consult, and recruit deep sector expertise in the ISU; and
 - publish contemporary guidance to provide helpful and efficient precedent to the market. It is likely to be most helpful if such information is published swiftly rather than collated in an annual report of the ISU's activity.
7. For investors, the usability of sector definitions will boost certainty of the UK's regulatory environment and of the impact of exiting investments, and thus assist decision-making.
8. The rationale for each of the definitions is also very helpful and we encourage the government to keep this updated for future changes or reviews.
9. A dual approach seems to have been applied to defining the scope of sectors. While we recognise the challenges involved, this inconsistency creates uncertainty as to the policy intention. A more consistent approach across sectors would increase understanding for businesses, investors and professional advisers. It will also enable more accurate and proportionate resourcing of the Investment Security Unit.
10. Under one approach, some proposed definitions, such as Advanced Materials, are very detailed and precise. This approach could result in omissions (eg of subsectors). On the other hand, in the absence of contextual overlay, some definitions may be an inefficient catch-all. To illustrate, under Advanced Materials, d. Technical textiles, iii. Materials (Feedstocks and constituents), 6. Breathable fabrics that have a range of qualities including having a good stretch, lightweight and weather resistant, businesses that design or manufacture such fabrics, or distribute or retail products (eg raincoats and sportswear), would seemingly be among those required to notify a transaction. Is this the policy intention?
11. In the second approach, definitions such as Artificial Intelligence, are more general and wide-ranging. One university's start-up team told us *'almost everything I do and start-ups I form could be caught by one or more of these definitions. The AI definition in particular will cut across most sectors as AI is part of most new start-up activity'*. Excessively wide drafting of definitions together with the severity of penalties for failure to notify will lead to over-notification.
12. There will need to be ongoing engagement (informal contact and discussion) between ministers and areas of the economy that are reliant on technology and/or rapidly developing, to ensure that sector definitions are future-proof.

13. There is a strong case for a system for advance clearance, as the new NSI regime has implications for a vast number of M&A and investment deals in the UK. With the net being cast so wide, the government should ensure that all those transactions which have no bearing on national security pass through the assessment process as quickly as possible – this will require an appropriately resourced ISU with deep sector expertise and timely Market Guidance including precedent information relevant to the assessment of assets, supply chains and acquirers.

Advanced Materials

14. We have the following observations on the proposed definition:
- The inclusion of sub-sector 2.d. Technical textiles, merits more explanation in the Rationale, so that the relevance is clearer. The functions, as set out in 3.d, catch an extraordinary range of materials.
 - In 3.f.i.1, the functions of Semiconductors could be more specific so as not to capture ‘innocent’ systems, equipment and components.
 - The functions of Phototonic and Optoelectronic materials in 3.g.i.2-3 would appear to catch mirror backing and glass. Is this intentional?
 - The functions in 3.j.iii of Critical materials, niche materials and materials related products would appear to catch many paints and foams. Is this intentional?

Data infrastructure

15. We have the following observations on the proposed definition:
- Entities under 1.a and 2.d would include virtually any entity with a software network. Is this the intention?
 - As drafted, the definition of relevant data in 3 would appear to create a separate need for notification. Is this intended?

Energy

16. We have the following observations on the proposed definition:
- Under 1.c, what is the significance of ‘reliable’ electricity and gas supply?
 - In 1.f.i, such undertakings would also catch small wind farms, and a de minimis threshold should be considered.

Transport

17. There appears to be a typo in 1; ie, the reference to paragraph (2.c) should probably be replaced with (2.d).

Question 3 To what extent do these definitions include the areas of the economy where foreign investment has the greatest potential to cause national security risks?

18. We do not comment on the completeness of the areas identified. Without suggesting that the following merit inclusion for mandatory notification, the relevant Rationale could refer to any considerations that the government has given to: the Internet of Things; distributed ledger technology; various ‘techs’, where technology is used to improve delivery of services, including EdTech, FinTech, MedTech; insecticides; gene therapy; and wider drugs industries.
19. In relation to this question, we believe guidance should be provided on whether a business is responsible for notifying activities or subsectors that they identify may carry a potential risk to national security but that are not defined.

Question 4 How else, aside from mandatory notification under the NSI regime, can the Government ensure relevant transactions receive appropriate screening while minimising the impact on business?

20. We refer to paragraphs 5 and 6 of our response which set out the need for government to educate businesses; appropriately resource the ISU; and publish timely precedent information.
21. The government should establish channels with the business and investment advisory communities to provide them with insights as well as to understand developments in the investment landscape. This can be achieved via professional bodies and trade organisations whose members (advisers, investors and businesses) operate in the 17 mandatory notification sectors. Initially, there should be engagement to refine and/or improve the definitions.

Question 5 Do these definitions strike the right balance between safeguarding national security and minimising the burdens placed on businesses and investors? Is it possible to narrow the scope of the definitions without compromising national security?

22. We refer to paragraphs 9 to 11 and 14 to 19 for examples of how definitions can add to the burden on businesses and investors.

SECTOR SPECIFIC QUESTIONS

ADVANCED ROBOTICS

Question 7 Are there opportunities to refine this definition to avoid capturing low risk advanced robotics, such as those that are less sophisticated or found in domestic application?

23. We think that case-by-case review may be most efficient given low volumes involved.

COMMUNICATIONS

Question 12 How can the definition be narrowed to exclude private communications networks that do not pose a risk to national security?

24. Consideration should be given to excluding the following:
 - private intracompany networks; and
 - businesses that do not sell but merely use private communications networks.

CRITICAL SUPPLIERS TO GOVERNMENT

Question 16 Are there alternative ways to ensure notification of relevant transactions, for example through contracts?

25. It is unclear what is envisaged under the proposed alternative ie 'through contracts', and it would appear to catch most commercial arrangements.