

March 2021

## UK Government provides more clarity on the scope of the National Security and Investment Bill

On 2 March 2021, the Department for Business, Energy & Industrial Strategy ("BEIS") published the results of, and its response to, the public consultation ("Consultation") on the 17 sectors that will fall within the mandatory notification regime when the [National Security and Investment Bill \("NSIB"\)](#)<sup>1</sup> is passed into law.<sup>2</sup>

The aim of the Consultation (which closed on 6 January 2021) was to determine whether the proposed sector definitions were sufficiently clear in their scope and application. Various stakeholders had raised issues on this,<sup>3</sup> specifically that the sector definitions originally proposed were drafted too broadly, would capture too many deals (many that would not actually involve any national security concerns) and would make it difficult for parties to

self-assess whether or not a mandatory notification was required in respect of any particular acquisition.<sup>4</sup>

The Consultation prompted 94 formal written submissions from various parties including law firms, investors, trade associations and even an unnamed regulator. BEIS has now reviewed and taken into account these submissions, indicating that it is committed to a "robust and proportionate approach to investment in the UK" and has therefore "significantly narrowed the definitions" of many of the 17 sector definitions under the mandatory regime.

Although, BEIS has indeed provided some welcome clarity and more certainty for parties contemplating deals that could potentially fall within the mandatory notification regime, the Government will still engage throughout 2021 with stakeholders directly as it continues to develop and refine these definitions (albeit not via a formal consultation process).

The definitions will remain in draft for the time being and may change as the NSIB makes its way through Parliament. Once the new regime comes into force, these sectors will be kept under review and updated as necessary through secondary legislation to address any new national security risks.

The NSIB is currently making its way through the House of Lords and is now expected to enter into force in autumn 2021, rather than spring 2021, as previously anticipated.

The key points to note following the response to the Consultation are set out in the rest of this Briefing.

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<sup>1</sup> Please also see our previous briefing on the NSIB: [the-uk-introduces-audacious-new-national-security-and-investment-bill---december-2020.pdf \(shlegal.com\)](#)

<sup>2</sup> Department for Business, Energy & Industrial Strategy. *National Security and Investment: Sectors in Scope of the Mandatory Regime – Government Response to the consultation on mandatory notification in specific sectors under the National Security and Investment Bill*. 2 March 2021. Available at: [National Security and Investment: Sectors in Scope of the Mandatory Regime - government response \(publishing.service.gov.uk\)](#)

<sup>3</sup> The City of London Law Society ("Law Society") was particularly critical, noting that the scope of the mandatory regime was disproportionate to, and at odds with, the Government's stated expectation that relatively few cases in the UK would give rise to any national security concerns. Apart from anything else, the Law Society anticipated that the sheer volume of notifications that would follow from the present drafting of the 17 key sectors would inevitably lead to process delays which "could portray the UK in a bad light". See: The City of London Law Society. *National Security and Investment: Sectors in Scope of the Mandatory Regime – Consultation on secondary legislation to define sectors to mandatory notification in the National Security and Investment Bill*. January 2021. Available at: [NSI-Sectoral-Consultation-Response-from-CLLS-and-Law-Society-Joint-Committee-06-01-21.pdf \(citysolicitors.org.uk\)](#)

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<sup>4</sup> Department for Business, Energy & Industrial Strategy. *National Security and Investment: Sectors in Scope of the Mandatory Regime – Government Response to the consultation on mandatory notification in specific sectors under the National Security and Investment Bill*. 2 March 2021. Para 21. Available at: [National Security and Investment: Sectors in Scope of the Mandatory Regime - government response \(publishing.service.gov.uk\)](#)

## The List of Key Sectors Remain Unchanged

First and foremost, an important point to note from BEIS' response to the Consultation is that none of the 17 key sectors have been removed and no new ones have been added. The overall list of key sectors remains almost entirely unchanged from when they were first published and are considered to be the right ones to include in light of the potential national security risks that each sector can raise. On this basis, it is now a matter of ensuring that the proposed definition of each one is sufficiently refined and clear.

## Intragroup Transactions

BEIS has rejected any suggestion that the NSIB should not apply to internal or intra-group transactions given that they still consider that such transactions may be capable of raising potential national security risks. The likely rationale behind this is to give BEIS the opportunity to ascertain any foreign entities or persons that might have an existing interest in companies currently operating in the UK. However, this position is at odds with the approach under competition laws where intra-group arrangements are outside the scope of antitrust rules under the *single economic entity principles*.

## Changes to the Definitions

Whilst not all the proposed definitions have been revised significantly, the following points are of particular note:

### 1. Advanced Materials

The revised definition identifies the same core categories (advanced composites, metals and alloys, engineering and technical polymers and ceramics, technical textiles, metamaterials, semiconductors, photonics and optoelectronics, graphene and related materials, nanotechnology and critical materials). However, the lists under each category are now much more extensive. Businesses operating in this sector should carefully review this new sector definition.

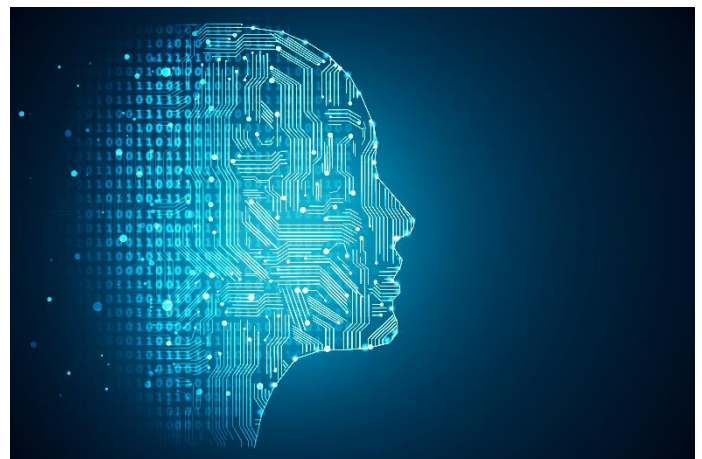
### 2. Advanced Robotics

This definition was previously very broad and raised the concern that the original definition captured virtually any organisation developing, producing or using sophisticated machines. It now concentrates on autonomous and semi-autonomous machines and contains important carve-outs for consumer products (such as robotic toys and "smart" vacuum cleaners), industrial automation systems and immobile devices.

### 3. Artificial Intelligence ("AI")

This was one of the more contentious key sectors, with some respondents arguing that AI is an underlying technology as opposed to a key sector on its own. The use of AI technology is becoming more and more ubiquitous and relied upon on by many industries where there will be no national security concerns. Indeed, the Law Society noted that a "*very large number of businesses in the UK*" now develop or produce goods, software or information that use AI to perform a complex task.<sup>5</sup> The original proposed definition would also have extended to situations where the entity in question has no control over, or access to, the relevant AI technology but rather benefits from the same under a separate licence agreement.<sup>6</sup>

As a result, BEIS have now narrowed the definition to focus on three higher risk areas where AI technology is used, namely: (a) the identification of objects, people and events; (b) advanced robotics; and (c) cyber security (noting that the Secretary of State may exercise his/her call-in powers in respect of qualifying transactions outside of these three applications). It is also now made clear that those who purchase products or licenses in relation to AI (for use but not for further development) are not covered. However, it is also clear that the definition is not limited to AI companies, but also captures companies in other industries which develop their own AI applications. The intention here is to provide greater clarity for investors, reduce the burden on industry and support the Government's ambition to grow the UK AI economy.



<sup>5</sup> The City of London Law Society. *National Security and Investment: Sectors in Scope of the Mandatory Regime – Consultation on secondary legislation to define sectors to mandatory notification in the National Security and Investment Bill*. January 2021. Para 2.25. Available at: [NSI-Sectoral-Consultation-Response-from-CLLS-and-Law-Society-Joint-Committee-06-01-21.pdf \(citysolicitors.org.uk\)](#)

<sup>6</sup> Ibid. para 2.26.

#### 4. Civil Nuclear

Amendments to this definition of the civil nuclear sector are primarily clarifications following comments from third parties (e.g. that it applies to all tenants of civil nuclear sites, regardless of the type or level of activity undertaken on the site). The Government has also confirmed that holders of non-nuclear radioactive material are not included within the scope.

#### 5. Communications

For the purposes of drafting this proposed definition, BEIS borrowed many defined terms and concepts from the Communications Act 2003. However, many respondents raised concerns that these existing terms were still too broad and risked applying to many different companies, including those in the various supply chains who would not have any direct involvement in the provision of an electronic communications network or service.

As a result, BEIS has now confirmed that the sector applies only to entities who are involved in the provision of communications networks, services and associated facilities wholly or mainly to members of the public.<sup>7</sup> Moreover, associated facilities are only caught by reference to a public electronic communications network or service which meets specified turnover thresholds. Entities which fall under this category will be: (i) providers of submarine cables systems; (ii) cable landing stations; and (iii) the operators of essential services in the digital infrastructure subsector. The latter encompasses top level domain name registries, domain name system resolver and authoritative hosting services, and internet exchange points. The Government has further indicated that it is actively considering a number of further amendments to this sector definition.



<sup>7</sup> BEIS has taken the drafting for this from Section 151(1) of the Communications Act 2003.

#### 6. Computing Hardware

The Government has refused to exclude consumer products from the definition, despite requests to do so, on the basis of the potential dual-use application of computing hardware products. This notwithstanding, the definition has been clarified and narrowed in a number of ways. For instance, some terms have been removed given they were not clear (e.g. functional capability) and others further clarified (e.g. computing processing unit) so as to minimise the risk that they could be misinterpreted. The Government has said that it will engage with industry in order to further refine this definition.

#### 7. Critical Suppliers to Government

The Government rejected calls to remove this sector from the scope of the mandatory notification requirement, despite the original definition appearing to capture a substantial range of suppliers of generic products and services. However, the definition has nonetheless been substantially narrowed to reflect these comments, focusing on the protection of classified materials, estates and people who work with such materials that could raise a national security risk. The scope of the term "*Government contracts*" has been clarified and is limited to "*contracting authority*" contracts (i.e. contracts with the State, central government authorities, regional or local authorities and bodies governed by public law), thereby excluding any contracts with institutions that have the Government as a shareholder. Further, subcontractors are no longer included in order to ensure a more proportionate approach.

It is worth noting that BEIS also refused to publish a list of critical suppliers on the grounds that this would be subject to change and such a disclosure could itself pose a national security risk.

#### 8. Critical Suppliers to the Emergency Services

The Government considers this as one of the most sensitive sectors. The revised definition incorporates definitions such as "*operational*", "*critical*" and "*IT infrastructure*" as well as suggestions on specific items that should be included, with the aim of refining and clarifying each category of goods. The Government has stated that it intends to continue to engage closely with stakeholders with a view to producing a narrower definition, including materiality thresholds.

#### 9. Cryptographic Authentication

The proposed definition of this sector has been amended to remove products that are ordinarily sold to consumers and to ensure that only products which



pose a national security risk are captured. It is intended to only capture entities that research, develop or produce products whose primary function is authentication using cryptographic means, where these products are to be used in systems critical for national security (i.e. the company provides the technology to UK third parties, such as government, critical national infrastructure or strategic industries).

## 10. Data Infrastructure

This sector definition now removes entities that merely own the site or building that houses data infrastructure, rather than the infrastructure itself. In addition, most data infrastructure will fall within the definition only if it is the subject of a direct contract with a "critical sector" entity to store, process or exchange that critical sector entity's data. Critical sector entities will be those public sector contracting authorities or entities that would be subject to mandatory notification under the 'Civil Nuclear', 'Critical Suppliers to Government', 'Critical Suppliers to the Emergency Services', 'Defence', 'Energy' or 'Transport' sectors.

## 11. Defence

The Government has once again rejected calls to define "national security", even in the context of the 'Defence' sector, and has confirmed that the definition could capture contractors or subcontractors who are providing services such as catering or cleaning to defence or national security facilities. The basis for retaining such a broad scope is the consideration that such contracts could provide access to sensitive facilities and that, as such, potential (though unspecified) national security risks could still ensue from this access.

## 12. Energy

In direct response to concerns raised from stakeholders, BEIS has clarified that *retail* electricity suppliers are not caught under this sector and all references to supply and suppliers have been removed. That is to say, those entities which offer electricity services, rates and other related products to residential and business customers but who do not actually own or control any infrastructure/generation assets will be excluded. Though this is a welcome clarification, the thresholds for what constitutes, for instance, an Authorised Electricity Operator in Great Britain (although not Northern Ireland) remain rather low.<sup>8</sup> Therefore, it is still likely that entities with any

<sup>8</sup> Specifically, "Authorised Electricity Operators" means any person (other than the licensee) who is authorised to generate, participate in the transmission of, distribute or supply electricity or participate in the operation of an interconnector.

physical assets which are connected with the upstream or downstream generation of power for energy purposes will remain caught by this sector. Electricity aggregators have been included.

In terms of petroleum infrastructure and pipelines, only those that meet certain throughput thresholds in the first year will be captured. The capacity threshold vis-à-vis a downstream petroleum facility has been increased from 20,000 to 50,000 tonnes.

BEIS has noted that further amendments to this sector are likely before the NSIB ultimately passes into law and it remains to be seen how much further it may look to refine this proposed definition in order to provide greater clarity on defined terms as well as how thresholds will be measured and over what period. Nonetheless, BEIS has made clear that its intention is to capture primarily those entities with a "key role in overseeing or operating any part of the GB electricity and gas markets" in Great Britain.



## 13. Military and Dual-use Technologies

The Government has rejected the suggestion that dual-use items made for UK markets alone should not come within the mandatory notification regime. However, the definition has been amended such that it now covers "researching, developing or producing restricted goods or restricted technologies". Further, the mere holding of information capable of use in connection with the development or production of restricted goods has been deleted.

## 14. Quantum Technology

There was significant feedback that this definition was too broad and would capture the majority of

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Authorised Electricity Operators will be within the scope if they provide "load" via: (i) individual assets that would have a total installed capacity, greater than or equal to 100 megawatts; or (ii) assets that, when cumulated with those of the affiliated undertakings of the acquiring entity, would have a total installed capacity, greater than or equal to one gigawatt. The definition of "load" is taken from the Grid Code as meaning the "Active, Reactive or Apparent Power, as the context requires, generated, transmitted or distributed".

transactions in this sector, including those involving the academic research community and associated supply chain sectors. The revised definition therefore focuses on capturing entities that develop or produce quantum technology products; thereby excluding pure research into quantum technology and entities that merely use quantum technology to supply services. The Government will continue to work with experts in this sector to further refine the definitions to be included in final regulations.

### 15. Space and Satellite Technologies

This sector has been narrowed to remove the provision of telecommunications and internet services via satellite from scope. The new definition also makes more explicit references to the focus on national security, by referring to the use of space-derived data for any military or national security purpose.

### 16. Synthetic Biology

There was a significant concern voiced from stakeholders that the original sector title (i.e. 'Engineering Biology') was too broad and would in effect capture all foreign investment in this sector. As such, the revised sector title now focuses specifically on synthetic biology. Moreover, the proposed definition of the same now makes clear that gene editing, gene therapy and DNA manipulation are included, but there are also now a number of activities that are expressly excluded for non-critical activities, including bioremediation, clinical diagnostics, food production (e.g. lab-grown protein) and therapeutic gene therapy. It seems that part of the reason for including 'Synthetic Biology' under the mandatory regime is because of its technological complexity which would make it difficult for the Government to comprehensively monitor the sector well enough to proactively 'call-in' transactions that are not routinely notified.



### 17. Transport

This sector has always been limited to ports, harbours and airports. BEIS made clear from the outset that it will not apply, for instance, to the rail sector or public services like buses or trams. That said, BEIS has addressed various concerns by making amendments such as the following:

- a) In relation to ports and harbours, BEIS has removed from the scope any mention of passenger capacity. Previously, the definition applied to ports or harbours which (*inter alia*) could handle vessels large enough to transport 12 passengers or more. This criterion would have been met by an inordinately large number of ports and harbours, many of which would have had no connection (actual or otherwise) with activities capable of raising national security concerns. Now, however, the definition has been tightened to refer to entities who own or operate ports and harbours (or related infrastructure) that handled 1 million tonnes or more of cargo in the year preceding the transaction. This definition is far more apt and clear in its scope; and
- b) In relation to airports, BEIS have clarified that only entities who have "overall responsibility for [airport] management" or are otherwise involved in traffic control operations are within the scope. Helpfully, this has ruled out the possibility that any company which has any operations at all within an airport might be caught, such as baggage handlers.

### Final Comments

Whilst some key concerns around the 17 sector definitions have been addressed (not all have been addressed) which should hopefully limit the number of notifications that are being made by parties (out of a sheer abundance of caution), the fact remains that some of the sector definitions are still broad and open to interpretation.

Therefore, the number of notifications BEIS receives once the NSIB passes into law may still be substantial. Indeed, concerns raised by stakeholders such as the Law Society may still continue to be relevant, not least the concern that the inevitable procedural delays and uncertainty will cause a flight on investment appetite in the UK, something that will be crucial to the economy's recovery as it starts to emerge from the COVID-19 pandemic.

Importantly, as explained earlier, BEIS has stressed that all the proposed sector definitions remain in draft form until such time as the NSIB becomes law. Consequently, it is quite possible that we may see

further changes to the proposed definitions of the 17 key sectors before the NSIB receives Royal Assent. BEIS anticipates that the finalised definitions will be set out in such supplementary legislation “as *Parliamentary time allows*”. It is helpful that BEIS have confirmed the proposed definitions will ultimately be written into statutory law, as it means that the sector definitions will be less of a moving feast after this time, where any amendments to them will need to be made through separate statutory instruments.

Indeed, the Government has also announced a series of policy statements concerning the various statutory instruments that will need to be passed once the NSIB receives Royal Assent. One such piece of legislation will concern the 17 key sectors, as noted above, whilst others will focus on (*inter alia*) the prescribed form for mandatory and voluntary filings, the factors the Secretary of State will consider when deciding to issue a ‘call in’ notice and precise guidance as to how penalties will be calculated. Whilst it is comforting to know that these supplementary statutory instruments will provide clarity on these issues, it also demonstrates the volume of secondary legislation that will need to be passed even after the NSIB comes into force.

More broadly, the overall NSIB regime itself continues to face much criticism. A recent report by the Foreign Affairs Committee (“**FAC**”) raised a number of concerns on the NSIB, including that BEIS’ anticipated review process will be too opaque and that the introduction of the regime would create a significant risk of politicisation over UK investments.<sup>9</sup> The FAC’s report also agreed with the Law Society’s view that the volume of notifications would greatly exceed the (already significant) 1,000 – 1,830 per annum that BEIS expects.

BEIS’ aim is to create a mandatory notification regime under the NSIB that is clear and proportionate. BEIS’ response to the Consultation has moved closer to achieving the former objective, but whether the latter can be achieved still remains to be seen.

## Contact us

If you would like to know about any of the issues raised in this briefing, our Competition Team would be happy to speak to you.



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<sup>9</sup> House of Commons Foreign Affairs Committee. Striking the balance: Protecting national security through foreign investment legislation. Sixth Report of Session 2019-21. 12 January 2021. Available at: [The FCDO’s role in blocking foreign asset stripping in the UK \(parliament.uk\)](https://www.parliament.uk/publications/2020/12/12)