

Takeaways For Transaction Parties After UK Acquisition Block

By **John Schmidt, Ronald Lee and Ludovica Pizzetti** (December 12, 2022)

On Nov. 16, the U.K.'s secretary of state for Business, Energy and Industrial Strategy blocked Nexperia BV's acquisition of Newport Wafer Fab on national security grounds.

This is the latest in a still relatively small set of prohibition decisions under the National Security and Investment Act 2021.

As we approach the first-year anniversary of the U.K.'s investment screening regime, we take stock of what this decision means for the early trends that are emerging and consider what it means for the year ahead.

This is the first time the U.K. government used its retrospective powers to order a divestment of a completed corporate acquisition under the NSIA. The acquisition completed in July 2021, before the NSIA came into force, when Nexperia increased its stake from 14% to 100%.

The Department for Business, Energy and Industrial Strategy called in the acquisition using its retrospective review powers. Although the purchaser was a company incorporated in the Netherlands, it is ultimately controlled by the Chinese group Wingtech, a Shanghai-listed company whose shareholders include those with links to the Chinese government. The target, Newport Wafer Fab, is the UK's largest chipmaker and manufactures silicon wafers that are also exported to Asia to be made into chips.

The U.K. government called in the transaction for review in May 2022 and, after a six-month-long review following various extensions of the review timetable, ordered Nexperia to reduce its shareholding in the target to at least its original, noncontrolling holding of 14%.

The ability to review and ultimately block transactions in certain sensitive sectors — particularly where the identity of the acquirer may raise national security concerns — was the purpose behind the new legislation.

The U.K. government is carrying out in-depth reviews particularly over Chinese investments in sensitive areas and is making use of its powers to order divestment.

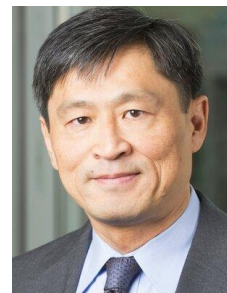
All three transactions the U.K. government has blocked to date have had links to China: two of them had Chinese acquirers — respectively, Beijing Infinite Vision Technology Co., Ltd. and Super Orange HK Holding Ltd. — and the Nexperia decision concerned an acquirer that was ultimately owned by a Chinese group.

That said, transactions undertaken by acquirers headquartered in countries that are close allies of the U.K. are not immune from close scrutiny. Experience shows that acquirers from countries such as the U.S., France or Israel may still give rise to a U.K. national security issue where the target business is engaged in sensitive activities.

Notably, for example, although reviewed under the previous regime, the proposed acquisition of U.K.-based chip design company Arm by the U.S.-based Nvidia Corp. was abandoned in February 2022 after it faced close scrutiny due to the significant national concerns identified by the UK Government.



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In fact, even a U.K.-to-U.K. deal may trigger a filing, as was the case in the acquisition over U.K.-based Sepura Ltd. by U.K. private equity firm Epiris, which was cleared subject to conditions on July 14.

The U.K. national security review regime is very much a black box process. Unlike a Competition and Markets Authority review that is an iterative dialogue between the notifying parties and the case team, a national security review involves little, if any, dialogue between the case team and the notifying parties. A filing is submitted where questions are asked, responses need to be provided and at the end of the process a decision is issued.

Clearances are not public and decisions involving remedies are extremely brief. The written decision in Nexperia is also brief and simply refers to national security risks related to technology and know-how that could result from a potential reintroduction of compound semiconductor activities, and the potential for those activities to undermine U.K. capabilities.

The decision also states that the location of the site could facilitate access to technological expertise and know-how in the South Wales Industrial Cluster,^[1] and the links between the site and the cluster may prevent the cluster being engaged in future projects relevant to national security.

The opacity of the review extends beyond the initial examination and the decision-making process to the negotiation, or, more accurately, imposition of remedies. In this case, it is unclear how much interaction there was between the parties and the U.K. government on the remedies before the order was issued.

For its part, Nexperia expressed surprise at the decision and reported having offered wide-ranging remedies, including a pledge not to conduct the compound semiconductor activities of potential concern and to provide the U.K. government with direct control and participation in the management of Newport.

The extent to which the U.K. government considered the proposed remedies is likely to be tested on appeal.

What Does This Mean for the Regime in the Future?

Nexperia has indicated that it will appeal the decision. Strictly speaking this is not a full appeal on the merits, but a judicial review of the decision-making process. This means the judge will not decide whether they would take the same decision on the facts but will decide only whether the U.K. government acted irrationally, illegally or with procedural impropriety.

Although the judicial review will be relatively narrow, it will still be the first serious stress test of the new regime. One of the points that is likely to come under scrutiny is whether the parties have been given sufficient reasoning. If that is not the case it is likely that the decision maker will be able to re-adopt the decision and rectify the procedural errors.

It will be interesting to see how the court approaches the decision maker's margin of discretion when considering national security issues under the NSIA.

It seems likely that the decision maker has a very wide margin of discretion before a decision or the imposition of potential remedies becomes irrational.

This highlights the strategic considerations that parties have to evaluate when contemplating transactions in high-risk and not so high-risk areas. It adds a further layer of complexity, risk and possible delay into corporate dealmaking, including the possibility

that the Department for Business, Energy and Industrial Strategy may call in deals that have already closed without prior notification under the NSIA.

Foreign Direct Investment in an Era of Multiple National Security Review Regimes

The Department for Business, Energy and Industrial Strategy's action is not out of kilter with the trend in other countries around the world, many of which are increasingly seeking to review and in some cases prohibit foreign control of foreign-strategically important industries.

For example, in late 2020, the French government blocked the acquisition of a French photo-sensor imaging technologies company, Photonis Technologies SAS, by a U.S. company, Teledyne Technologies Inc., and in April 2021, the Italian government blocked a Chinese takeover of a semiconductor company, LPE Spa.

It is also about the particular industry sector and many other factors besides the nationality of the acquirer: The semiconductor supply chain has already been the subject of two out of the three decisions to have been blocked under the NSIA.

The abandoned acquisition of U.K.-based chip design company Arm, as mentioned, also concerned the semiconductor industry. Other sectors where the U.K. government has also taken a critical look for possible national security concerns include defense, dual-use, artificial intelligence and data infrastructure.

Finally, the Wall Street Journal reported discussions between U.S. and U.K. officials on the subject. It says that unwinding the deal was also Washington's preference as it could help the U.K. become an important part of the supply chain for electric vehicles, although there was no U.S. government request to unwind the deal.

This report underscores the importance of wider political considerations in such processes and particularly for dealmakers of coordinating their foreign direct investment and national security strategy across national lines.

It also underscores the importance of an aligned strategy across the Atlantic in such cases, even though the U.S. and U.K. regulatory regimes are distinct and different in many respects.

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[1] <https://www.swic.cymru>.