Client Alert | Antitrust/Competition

Reduced merger control thresholds for protection of national security

11 June 2018

Authors: Marc Israel, Sophie Sahlin, Rebecca Yourstone

Overview

Today, 11 June 2018, new merger control rules entered into force in the UK for mergers where the business being acquired (**Target**) is active in one of three specified sectors. The new rules apply where the Target is active in: the production or development of military or dual use goods; quantum technology; or computing hardware (together the **Specified Sectors**).

The primary purpose of the new rules was to reduce the thresholds allowing the UK Government to intervene in mergers in the Specified Sectors on the grounds of national security. However, they also allow the Competition & Markets Authority (**CMA**) to review acquisitions of a business active in any of the Specified Sectors on competition grounds.

For transactions involving a business that is active in any of the Specified Sectors the UK turnover threshold is lowered from £70 million to £1 million, and the current share of supply threshold of 25% no longer requires there to be an overlap in the parties' activities, but can be met by the Target alone (**Reduced Thresholds**). Consequently, the Reduced Thresholds will enable political intervention in cases raising potential national security concerns even where a company with very low revenues in the UK.

Background

Previously, the UK Government could only intervene in mergers on national security (and other, specified, limited) grounds where a "relevant merger situation" existed. This meant that the Government's possibility to intervene was, prior to the introduction of the Reduced Thresholds, limited to transactions where the 'regular' merger thresholds set out in the Enterprise Act were met, i.e. where:

- the business being acquired had a UK turnover exceeding £70 million (**Turnover Test**); or
- the merger would result in the creation of, or increase in, a combined share of supply of particular goods or services in the UK (or a substantial part of it) of 25% or more (**Share of Supply Test**).

This meant that the Government could only intervene in transactions on national security grounds where one of these jurisdictional thresholds was met[1]. There was therefore perceived to be a gap in the Government's powers to intervene in cases that might have raised national security issues (if one of the parties was not a defence contractor). Consequently, the Department for Business, Energy & Industrial Strategy (**BEIS**) published a National Security and Infrastructure Review Green Paper (**Green Paper**) in October 2017, and consulted on its plans to introduce the Reduced Thresholds.

On 15 March 2018, BEIS published the Government's response to the Green Paper, in which it confirmed its intention to amend the jurisdictional thresholds to enable more effective protection of national security. Various changes were made in relation to the definitions of the Specified Sectors that would be covered by the

[1] The Enterprise Act allows the Government to intervene on national security grounds even where the jurisdictional tests are not met if one of the parties is a "relevant government contractor", essentially where one party is a defence contractor.

application of the Reduced Thresholds but, essentially, the Government's decision was to implement its proposals as set out in the Green Paper.

New thresholds

The application of the Reduced Thresholds to cases involving the military and dual-use goods will be made by reference to Strategic Export Control Lists, and the Government intends in due course to publish detailed guidance about these lists to assist parties in determining whether the Reduced Thresholds apply. The statutory instrument introducing the Reduced Thresholds also contain detailed, and fairly complex, definitions of activities that are covered by quantum technology and computing hardware. There will inevitably be some uncertainty, especially at the outset, to determine whether a Target's activities are within the Specified Sectors and so the Government has stated that parties will be able to discuss a proposed transaction with the Government department that has responsibility for their sector.

Today, to coincide with the entry into force of the Reduced Thresholds, the CMA has issued guidance on its approach to changes to the jurisdictional thresholds for UK merger control (**Guidance**). In particular, the Guidance states that although the CMA is now able to review mergers that meet the Reduced Thresholds on competition grounds (whether or not the Government intervenes on national security grounds) it does not intend to do so based solely because a deal can be caught by the Reduced Thresholds. Rather, as is currently the case, the CMA only expects to use its powers to investigate a non-notified merger if there may be a realistic prospect of a substantial lessening of competition arising.

The Guidance helpfully states that "*[f]rom a competition perspective the CMA does not believe that there is any need to treat mergers involving [the Specified Sectors] differently from mergers in other sectors*". It also notes that transactions that might be expected to raise competition concerns would typically already fall under the CMA's jurisdiction under the Share of Supply Test (i.e. due to an overlap in the parties' activities resulting in a share of supply of more than 25%). The CMA therefore "*does not anticipate opening any own-initiative competition investigations on the basis of horizontal concerns into transactions where it would previously not have had jurisdiction*". Whilst the Reduced Thresholds will permit the CMA to investigate 'vertical' mergers that it could not previously have reviewed (i.e. where the parties operated at different levels of the supply chain and so did not have overlapping activities and the target's UK turnover was less than £70 million) the Guidance notes that "*most non-horizontal mergers are benign and do not raise competition concerns*" and so does not expect the Reduced Thresholds to result in any material change to its approach to opening own-initiative competition investigations on the basis of non-horizontal concerns.

Notwithstanding the introduction of the Reduced Thresholds, the UK will continue to operate a voluntary filing regime, even for transactions in the Specified Sectors. This means that parties to a transaction will not need to seek prior approval for a deal (or confirmation that the Government will not intervene on national security or other permitted grounds) before closing. However, as has always been the case, there remains a risk that the Government could intervene (and/or the CMA could investigate a merger on completion grounds) post-closing[2]. It should, however, also be noted that the Green Paper sought views on whether the UK should introduce a mandatory and suspensory merger control regime for transactions involving foreign investment in the provision of a focused set of 'essential functions' in key parts of the economy, such as the civil nuclear and defence sectors which could raise potential national security concerns. The Government's response on whether to introduce a mandatory merger control regime for certain types of transaction is pending.

Comment

The Reduced Thresholds extend the UK Government's ability to intervene in cases in order to protect national security. By lowering the jurisdictional thresholds which allow intervention, a larger number of transactions will be potentially caught, especially the acquisition of companies involved in new technologies that may not yet have material turnover in the UK. In practice, the new rules are likely to make foreign acquirers (especially those from certain jurisdictions and/or controlled by foreign governments) of companies active in the Specified Sectors more difficult and subject to greater scrutiny. This may have implications for sellers when considering a transaction, especially if they are choosing between competing acquirers.

[2] Under the Enterprise Act, completed transactions can be reviewed up to four months after the later of details being made public or being brought to the attention of the CMA.

White & Case LLP
5 Old Broad Street
London EC2N 1DW
United Kingdom

T +44 20 7532 1000