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# **NSIA – Financial Markets Law Committee**

## **Banking Scoping Forum**

**24 January 2024**

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# OVERVIEW

## NATIONAL SECURITY AND INVESTMENT ACT

### Application in the context of Financings

Points for Discussion:

- Government Call for Evidence – closed 15<sup>th</sup> January 2024
- The Mandatory Regime:
  - Taking Security – issues when creating the security interest
  - Taking Security – issues when an event of default occurs
  - Taking Security – issues on enforcement
  - Insolvency – issues if appointment of a receiver or liquidator is required, rather than the appointment of an administrator
- Risks of Call-in where the mandatory regime does not apply

# NSIA – TAKING SECURITY OVER SHARES

## ACQUIRING CONTROL THROUGH SHAREHOLDING

- *A person gains control of an entity if the percentage of the shares that the person **holds** in the entity increases above certain thresholds (Sections 8(1) and 8(2) NSIA)*
- **Legal share security**
  - mandatory notification and pre-clearance required if entity (including overseas entity) whose shares are charged carries out specified activities in any of 17 specified sectors. Legal charges over shares are rarely used in England, but are mandatory in Scotland and common in other jurisdictions.
  - obtaining clearance can take up to 75 working days.
- **Equitable share security**
  - some debate over whether Security Agent/Lender **holds** shares but market approach is not to notify. This approach has been confirmed by BEIS and is supported by strict reading of the NSIA in terms of the terminology of company law which regards only the holder on the register as holding shares. However, the definitional language of NSIA is not ideal – see particularly s 8(1).
- **CLLS Submission on Call for Evidence**

Legal and equitable charges should be treated alike and creation of a charge should not require mandatory notification provided that the chargor continues to exercise voting rights and the rights of the chargee/security agent/trustee are limited to using voting rights for preservation of security (see Schedule 1, para 7). Request for interpretation of existing provisions to that effect.

## NSIA ENFORCEMENT PROCESS

Because of the position on acquisition of voting rights, LMA has changed the terms of its affected forms so that there is no acquisition of voting rights until approval under the Act has been obtained.

The vast number of historic security arrangements, however, contain automatic acquisition of voting rights immediately on default or on notice of default. This carries a risk of criminal prosecution for acquiring voting rights without prior approval if, at the time of enforcement, the security covers an interest of 25% or more in a 17 sector company..

Indications are that smaller deals continue to be done on automatic enforcement terms and this is very popular with lenders. Equally foreign parent companies and their advisers are likely to be unaware of the problem if contracting under foreign law.

As the status of a company at enforcement cannot be known when the charge is entered into – this means that enforcement risk affects entire market practice for secured loans to corporates, not just secured loans to current 17 sector companies/parents.

### CLLS Submission

Lenders should be able to acquire voting rights without mandatory prior approval at least for agreements entered into before a particular date. Arguing for a contemporary date.

Exercise of voting rights by or on behalf of chargee(s) should generally be permitted as part of enforcement without prior approval either under a generous interpretation of sched 1, para 7 or specifically, at least within a time limit. This would mean that market practice generally would not be disturbed and would aid British companies generally in obtaining secured finance.

## NSIA – ENFORCEMENT OF SECURITY OVER SHARES

- Enforcement of share security can take various forms, most of which would require prior mandatory notification and clearance if shares relate to an entity which carries out specified activities in the UK in any of 17 specified sectors.
- Examples:
  1. Actual exercise of voting rights e.g. to appoint a CRO (chief restructuring officer) or to replace the board as precursor to proposing a scheme of arrangement or otherwise to turn the business round
  2. Perfection of an equitable mortgage or charge to a legal mortgage
  3. Appropriation (i.e. transferring shares into the name of security trustee): rare unless financial collateral
  4. Sale of the shares to nominee or third party purchaser
  5. Appointment of an insolvency officeholder other than administrator.

### CLLS Submission

Enforcement should not require a mandatory pre-approval with regard to exercise of voting rights by or on behalf of chargee(s), only for a long-term change of control. This might be a limited permission eg for 6 months or a year, so as to allow prompt action to safeguard the business. Again distinctions might be made dependent on eg regulatory status or standing of chargee/security agent or security trustee.

**Together with other suggestions this would mean that only 3 and 4 of the examples above required a mandatory pre-clearance.**

# INSOLVENCY

## CHOOSING INSOLVENCY PROCESS

- **Receiver**
- Option that may be most suitable for an SPV and which may remain legally available – NSIA treats as acquisition, so it would require prior approval in case of 17 sector company
- **Administrator**
- NSIA does not treat as acquisition so can be used freely
- **Liquidator**
- NSIA treats as acquisition, so it would require prior approval in case of 7 sector company
- **CLLS Submission**
- All forms of insolvency process should be outside mandatory regime, at least when the official receiver or a insolvency practitioner is appointed. This will ensure that 17 sector companies have best chance of appropriate treatment for their business.
- Consideration should be given to allowing schemes of arrangements with creditors to be started (including use of voting rights by or on behalf of chargee(s)) on the basis that consent is only needed in advance of any actual changes of control resulting from the scheme – for the same reason and to reflect government policy on insolvency.

## NSIA CALL-IN RISK

### MATERIAL INFLUENCE AND ASSET CONTROL TRIGGERS

- *A person gains control of an entity if they are able materially to influence the policy of that entity (Sections 8(1) and 8(8) NSIA).*
- *A person gains control of a qualifying asset (land, tangible moveable property and certain IP) if they are able to use, direct or control its use (Section 9 NSIA).*
- Material influence and asset control triggers only apply to call-in regime.
- Apply to any sector of the economy if national security concerns raised but Statutory Statement confirms call-in for material influence most likely if entity carries out specified activities in one of 17 specified sectors or carries out activities closely linked to those activities and call-in for assets most likely if asset used in connection with such activities. These may be in the UK or abroad.
- It is possible that a loan agreement (or any other Finance Documents) confer material influence over an entity or give control over assets to the Lenders/Security Agent?
  - Material influence not defined but see CMA guidance.
  - *“Loans are unlikely to pose a risk to national security and so are unlikely to be called-in” (Paragraph 15 Statutory Statement).*
  - *“Land is mainly expected to be an asset of national security interest where it is, or is proximate to, a sensitive site” (Paragraph 36 Statutory Statement).*

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