HOUSE OF COMMONS

International Trade Committee

Oral evidence: Inward Foreign Direct Investment, HC 124

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Watch the meeting

Members present: Angus Brendan MacNeil (Chair); Mark Garnier; Paul Girvan; Sir Mark Hendrick; Anthony Mangnall; Mark Menzies; Martin Vickers; Mick Whitley; Craig Williams.

Questions 29 - 55

Witnesses

II: Camilla de Coverly Veale, Head of Regulation, Coalition for a Digital Economy; Dr Ashley Thomas Lenihan, Fellow, Centre for International Studies, London School of Economics; and Lawrence Slade, Chief Executive, Global Infrastructure Investor Association.

Examination of Witnesses

Witnesses: Camilla de Coverly Veale, Dr Ashley Thomas Lenihan and Lawrence Slade.

Q29 **Chair:** Now we will move over to panel two. I can see at least one familiar face. I can see Camilla de Coverly Veale, Dr Ashley Thomas Lenihan and Lawrence Slade. In a previous incarnation I was Chair of the Energy and Climate Change Committee, and Mr Slade had a different hat on. We have been in this sort of forum before.

I will ask you all to introduce yourselves—name, rank and serial number—starting with Camilla.

You are muted, Camilla. It gives me the opportunity to make my favourite joke, which is that mutations are the problem of this pandemic.

Camilla de Coverly Veale: There is always one, isn't there? It had to be me. I am so sorry. Yes, my name is Camilla de Coverly Veale and I am head of regulation for the Coalition for a Digital Economy, or Coadec for short.

Dr Lenihan: Hello, I am Dr Ashley Thomas Lenihan. I am a fellow at the Centre for International Studies at the London School of Economics, and I am also an associate at LSE IDEAS, the foreign policy thinktank. I should also note that I am head of policy and engagement at the British Academy of Management and a senior policy adviser at the Academy of Social Sciences, but I am here in my private research capacity from LSE.

Chair: Excellent, very accomplished indeed. Thank you, and Mr Slade.

Lawrence Slade: Thank you, Chair, good to see you again. I am Lawrence Slade, chief executive of the Global Infrastructure Investor Association, a membership body for international investors in infrastructure, with around 62 investment funds in membership.

Q30 **Chair:** Thank you. We are starting late, and I have to say that I will have to depart, unfortunately, given the travel difficulties that we have at this time. At some point I will pass the baton to Mark Garnier, who is more than able to run as fast and as far as anyone else, certainly the current Chair.

Dr Lenihan, as a scene-setting question, what is the key purpose of the National Security and Investment Act and its key provisions? How do they compare with other countries?

Dr Lenihan: Thank you, Chair, it is a good question.

Chair: Scene-setters can be tricky questions.

Dr Lenihan: Exactly, they can. Its immediate purpose is to create a new and comprehensive regime for the review of and the intervention into

investment transactions on national security grounds. Its overarching purpose, of course, is to better protect UK national security, in a context where concern has been rising steadily over strategic state-sponsored or subsidised foreign investments that are politically rather than market driven. That makes the Act a welcome and important step for protecting UK national security but also for bringing it in line with its allies as well.

The Act covers what it defines as trigger events, which are essentially notifiable acquisitions of control over qualifying entities, business entities and assets. What constitutes control is defined very thoroughly in the Act so I will not go through that. It varies a little bit under different parts of the regime but includes, in most instances, acquisition of shares or voting rights of an entity that crosses the 25%, 50% and 75% thresholds.

The Act creates a hybrid regime for assessing the national security implications of these trigger events, and that has three key components. First, it creates a mandatory notification regime for notifiable acquisitions in certain sensitive sectors. Those will be specified under further regulation later. What that means is that any acquirer of an entity or asset in what is currently proposed to be 17 sensitive sectors must first get the approval of the Secretary of State before completing their acquisition or it is void.

The second element of the Act is that it creates a voluntary cross-sectoral notification regime, and that just means that those involved in proposed or concluded trigger events that might pose a national security risk or might be perceived to present a national security risk in any sector not specified under that mandatory regime can voluntarily seek the approval of the Secretary of State.

The motivation for doing that comes from the third major component of the regime, which is the power of the Secretary of State to call in proposed or completed trigger event acquisitions to assess their national security implications for up to five years after the event.

Underpinning all of this, of course, is a very wide spectrum of remedies that are available to the Secretary of State to address any national security concerns posed by a particular transaction. That includes the ability to veto a transaction, to mitigate it by imposing certain conditions on it in a final order, and it also allows the Secretary of State to impose an interim order during the assessment process to prevent or reverse pre-emptive actions by the parties involved, or to mitigate its effect. There are also civil and criminal sanctions, which we will not go into, for non-compliance and provisions for judicial review.

How does that compare with other countries? I know we are short on time, so I am going to try to keep it short. To put things in perspective, the OECD estimates that there are about 48 countries, plus the EU, at least that have some sort of mechanism like this to protect sensitive and strategic assets from foreign control and manipulation. Each country has to have a unique approach to that necessarily because of their different

geopolitical, economic and domestic context, but there are some trends that we can compare in relation to the UK legislation.

Like the UK, many countries at the moment are amending existing legislation or creating entirely new regimes to cover investments in emerging areas of concern, particularly holders of sensitive data, advanced technologies, biotechnology, real estate near sensitive locations and other tangible and intangible assets that are sensitive.

Like the UK, many countries use this hybrid approach that blends cross-sectoral and sector-specific review regimes, as the NSI Act does, including close allies and peers like the US, Germany, Australia, and even competitors like China.

Where the UK legislation differs dramatically from most other review regimes is that it covers domestic as well as foreign investors. That will have a number of implications because the Government are likely to see a much higher volume of notified investments in the first few years than is usual for this kind of regime because in most large economies, with cross-sectoral review regimes and high levels of foreign investment, there is often a formalised, regularised system of input from different Ministries and Government Departments across different sectors to help monitor and assess that risk. That is something that the UK might want to consider establishing behind the Investment Security Unit as it goes forward. I am sure your next witnesses are going to talk a little bit about the caseload.

Chair: Thank you very much, that is appreciated. You might hear a bell in the background. It is for voting, but it does not apply to us all, happily. Some of us have proxies organised.

Q31 **Mark Garnier:** My question is to Camilla but, Ashley, could I quickly pick up on something you said earlier? You were talking about the provisions of the Act, looking at trigger points on equity investments. I sat on the Bill Committee on this so was asking technical questions. I would be very interested in your views on the fact that debt has been ignored in all this.

In certain circumstances, given the fact that equity investors obviously have a statutory right to vote and to make changes to the governance of a company, for example, debt investors—be they through bonds, overdrafts or just loans—obviously do not have a statutory position in terms of decision making, but in any practical sense if your bank manager or your debt holders are giving you a certain amount of debt at competitive rates they have a surprising amount of influence. Do you think this Act misses out on a whole area of influence that has not been defined through debt?

Dr Lenihan: That is a very good question. Emerging changes to regimes like this in other countries are increasingly looking at new modes of risk transfer and new modes of influence that strategic actors are using. This could be an emerging area. One of the things we have seen in the US, for example, is strategic actors, particularly the Chinese, in some cases are

buying bankrupt assets. Under this Bill that will be covered by the asset provisions, especially under the call-in procedure more so than probably the mandatory notification regime.

The Bill, as it has been amended slightly to lose that 15% threshold, might need to look in the future under regulations at dealing with non-controlling forms of influence of the type that you are talking about, if it turns out that that is a problem. Under the Bill, as I read it, it is something that can be amended later. I am not a lawyer but, as I read it and from my knowledge of other regimes, if that emerges to be a real problem, then it is something that can hopefully be dealt with in regulation, but it might need to be the case that we look at non-controlling investments down the road.

Q32 **Mark Garnier:** Personally, I think they have missed a trick. Angus is looking nervous about his flight, and I am going to have to take over in a minute. Thank you for that.

Camilla, the notification under the new Act is applied to 17 economic sectors, and your organisation raised the prospect of many irrelevant companies in sectors like AI being called in. Do you think the Government have tackled this properly? Have they addressed this in the revised sector definitions?

Camilla de Coverly Veale: First, I should say that we broadly support the aims of the Bill. We just think there is a scope and definitional issue. The short answer to your question is no. We think the new definitions pull a lot of irrelevant companies out of scope, so we are very happy about that, but we still think there are issues. For example, with artificial intelligence, as we understand it the Government are still interested in capturing and examining transactions that deal with AI that recognises objects, people and events, as well as AI to do with cybersecurity and advanced robotics.

The problem is that AI to do with cybersecurity and to do with recognition of objects, people and events is increasingly foundational to any business that wants to be successful right now. For example, we have had a lot of discussions with AI start-ups in specific niche sectors who are really concerned that they are going to be caught by this regime to their detriment. Take agritech, just to give you one quick example. We were talking to a start-up that has been teaching its AI to distinguish between a chicken and a cabbage to help farmers assess their livestock. They are worried that this is going to be captured by the new regime, and we just do not think this is what the Bill wants to capture, a chicken and a cabbage.

Q33 **Mark Garnier:** It does want to capture the principle of AI. I take your point on the animal, vegetable, mineral thing, which is the application of it. But the technology in the AI, is that what it is trying to get?

Camilla de Coverly Veale: As we understand it, yes. We just think there are lots of things that are going to be captured that just have

nothing to do with national security. They cannot be used for something else.

Q34 **Mark Garnier:** Lawrence, your association objected that, "Most of the 17 sectors are broadly defined". Are you any happier now, or do you think the Government are still not meeting your expectations?

Lawrence Slade: I would probably agree with quite a lot of what Camilla said. Although there has been a fair amount of change in terms of the structure and the 17 categories, we still think they are too broad. I could give you a quick example from the energy sector, for example, where generators with as little capacity as 100 megawatts, which is 0.1% of UK capacity, would be caught by this. It goes back to what Ashley was saying, the risk is that, instead of seeing tens or hundreds of deals caught by this, you end up seeing thousands of deals. Is there the capacity to deal with those in a timely fashion?

Q35 **Mark Garnier:** The issue is not the principle, it is that in any sort of sensible administrative thing you just will not be able to deal with it all.

Dr Lenihan: I understand what the regime is trying to do. It is a matter of how you do it. Particularly with new and emerging technologies, the mandatory notification regime, especially in the beginning, is trying to capture things that might not otherwise be caught. That is understandable.

On the issue of the high caseload volume, it might be worth doing something along the lines of what they did in the US after the 2018 legislation, which is they did a pilot programme where they tested—they had a broad number of sectors that they were trying to do mandatory notifications for in the technical, critical infrastructure TIC area. What they found was that using broad sector codes did not work because they captured a lot of things that they were not intending to capture, and they missed out on a number of other cases that did involve critical technology but did not sit in those sectors, like the agricultural AI example that was just given.

Instead of using these sector codes or sectors, they have now moved and are piloting the use of specific export-controlled technology, which might be just another way of thinking about it and looking at it as the regime grows and evolves. It might think about piloting something else other than just broad sectors.

Mark Garnier: I am going to come back later on the role of the Export Control Joint Unit as a separate thing. Angus, I will hand back to you.

Chair: I have another few minutes. I see Anthony Mangnall is back, which is fantastic because he was hoping to get in on this area.

Q36 **Anthony Mangnall:** Apologies to our guests. I am sorry that I had to step away.

Camilla, your organisations have both warned that the National Security

and Investment regime will lead to a huge volume of casework for the Government's Investment Security Unit. What is that going to mean, and are we clogging up the system with more bureaucracy and red tape?

Camilla de Coverly Veale: During the Bill's passage through Parliament we engaged extensively with the new Secretary of State and his team at BEIS. We were delighted when they amended the Bill and raised the trigger threshold from 15% to 25%, because we think that will bring out of scope a lot of the early-stage investments that we thought would absolutely deluge the new unit. We are very happy with that.

Yes, we think that, if not an impossible caseload, it is going to be a caseload that risks killing and collapsing deals. Tech start-ups live and die on their investment, so we are very worried about it. We think the Government have been incredibly naive in their estimates. We think this is going to come from three reasons. One is the broad sector definitions, which we have already discussed and I will not go back into. The next one is that the expansive definition of national security, the risk of criminal sanctions and of fines, will mean that we just think that, as a standard procedure, investors are going to voluntarily notify the new unit of their intention to do a transaction. That is the other issue.

The final issue is we worry that BEIS will not hire enough people or people with sufficient qualification to assess these deals. A lot in our industry question whether you can have someone who can assess these deals, and the Government already struggle to get tech experts anyway. They are going to struggle to find more.

Q37 **Anthony Mangnall:** This may be totally irrelevant, and please slap it down if it is not a good enough question. Under the Modern Slavery Act, the Government were asking companies to come forward with mission statements to say they were not committing slavery within their supply chains. To fulfil that obligation, all companies had to do is create a piece of paper saying they are not conducting modern slavery. The reality is it is not pragmatic, it does not prevent, and that is why you get examples of companies like Boohoo doing what they are doing.

Anything the Government do in this area is quite limited in terms of the response that we are expecting, because if we do not have the staff and if we do not have the people to be able to audit it and go through the proper thresholds, and make sure that we are getting our due diligence sorted, it slightly questions why we bother going to this extent because there are no punitive measures that stop companies from messing about. Sorry, I am on a high horse, but does that make sense to you?

Chair: It is a good high horse.

Camilla de Coverly Veale: The only difference between those two examples is that in one the company can carry on doing what they are doing but in this example they cannot, or their transactions are put in legal jeopardy. Anything that is going to risk deterring investment is something we are concerned about.

Q38 **Anthony Mangnall:** Just out of interest, the Modern Slavery Act is coming back and a few people are suggesting—and I have to declare my interest because one of them is me—that you expand the Modern Slavery Act to go beyond supply chains and also include investments. That would include outward investments as well as inward investments. Is that something that concerns you or pleases you? What is your view on it?

Camilla de Coverly Veale: I would not want to comment on it on this Committee because we have not prepared for it, but I will happily find out our position and write to you.

Anthony Mangnall: That would be appreciated. Thank you for your time.

Q39 **Sir Mark Hendrick:** I want to refer back to the so-called irrelevant companies that would be dragged in on the basis of AI. I cast my mind back to the Iraq supergun affair, which sounds totally irrelevant but I will make clear the relevance. Obviously, British weapons companies in the past were forbidden from selling heavy artillery to Iraq, and the Iraqis went to another company and ordered a long steel tube, which fulfilled the same purpose when it was exported to Iraq.

The AI company that Camilla mentioned, which was developing software that could tell the difference between a cabbage and a chicken, in terms of the data that that AI company is using it is obviously irrelevant to national security, detecting whether something is a cabbage or a chicken. But the pattern recognition algorithms and the technology that the software is using can probably be equally applied to things like racial profiling and recognition of one race of people from another. In authoritarian regimes very often some companies—I will not mention which countries—are using that type of software and technology to commit human rights abuses and it could possibly be used in warfare in future for a battle between one country and another.

So what, on the face of it, can seem a quite innocuous application, the same technology and algorithms could be used for something totally different. While it is very inconvenient for companies that are developing the software to be hauled in on the basis of national security, could Camilla perhaps comment on those other applications that could use the same technology?

Chair: Ashley also showed an interest in this one, but Camilla.

Camilla de Coverly Veale: I was only going to say that these technologies are not the same. It is not that if you teach it to see the difference between a chicken and a cabbage it is going to see the difference between two different people. They are not the same technologies.

Sir Mark Hendrick: I must disagree with you because it is not the data, it is the algorithms. The data will describe how a chicken looks and how a cabbage looks, but the same algorithms could be used for facial recognition and to distinguish between different races of the human race.

It is not the data, it is the algorithms and the type of technology. I know you are talking about machine learning. We can machine learn in that way as well with a different application.

Chair: We move now to Martin Vickers.

Martin Vickers: My question is to Dr Lenihan. One way in which the new—

Sir Mark Hendrick: Chair, you did call in Ashley on my question.

Dr Lenihan: I was just going to say that if you look at previous cases in other countries that have had to be vetoed—it is very rare when full transactions are vetoed—a great example is StayNTouch from a couple of years ago. It was essentially a hotel, travel and leisure company that collected data about where people stayed in different hotels, and it was software that was used by hoteliers. It does not seem like a national security issue, but it is because that data was live and real-time. The company was attempted to be bought by a Chinese Government-backed or supported company, it appeared. It was a huge national security issue when you think that it could track where Government employees, both domestic and foreign, were staying and their exact location at any given point in time.

Things that do not on the surface seem like they have another application often do, and the critical thing about this caseload issue is to have the right culture and the right staffing, capacity and feed-in from other Departments behind the ISU. That is the way you overcome it. I do not think you are going to be able to cut out a lot of these things that you are looking for.

Chair: Martin Vickers, can I invite you and apologise? This will be your third attempt out of the box. You were early out of the blocks in the closed session we had earlier, so this time the field is yours.

Q40 **Martin Vickers:** No problem, Angus. I have a question initially to Dr Lenihan. One way in which the new Act differs from comparable legislation in other countries is in respect of investments outside UK territory, the extra-territoriality. Can you explain how this aspect of the Act works and what its implications might be?

Dr Lenihan: You mean extra-territoriality in the sense that entities and assets, subject to review under the Act, include not just UK-based ones but also any foreign entity that carries on activities in the UK or that supplies goods and services to the UK, or assets that do the same. Yes, on the surface that does seem much wider in scope than many other existing regimes, but there is a very clear reason for its inclusion. It is not unprecedented, and we are going to see this in more regimes going forward.

The first thing is that foreign investment transactions can have implications for domestic national security if, for example, the entity or asset is a critical part of the state's defence supply chain or

infrastructure, no matter where it sits geographically. That is the first thing.

In the US, for example, the Committee on Foreign Investment in the United States, CFIUS, has in the past mitigated and blocked foreign takeovers of foreign-headquartered companies on national security grounds. In 2016, they blocked the sale of Lumileds Holding, a division of the Dutch company Philips, to a Hong Kong private equity firm, again on security grounds. They also mitigated in 2013, and this is a great example, the Chinese company CNOOC. It was bidding for the Canadian oil company Nexen, which had US-based assets. The mitigation that they were able to effect in their opposition to the deal was that it was only approved on the condition that CNOOC could not have operational control over Nexen's assets in the US that sat next to sensitive military bases, which makes sense.

That is the traditional use of extra-territoriality, and we have seen it in other countries. The OECD in a recent report from last year noted a recent trend of concern and more use of this extra-territorial provisioning over transactions that happen outside the country that involve the transfer of sensitive data, intellectual property, technology or technological applications, not just through sales but through divestments and the creation of joint ventures. That is because, as technology advances and our understanding of national security changes, these things are becoming increasingly delinked from physical geographical territories and where they sit. That is requiring many foreign investment regimes to adapt and move away from what has traditionally been a more territorial focus.

Again, the recent US 2018 legislation FIRRMA and the National Defense Authorization Act recognise this. You will see other countries moving in that direction, too. It does not surprise me. I think it will be used sparingly.

Q41 **Martin Vickers:** Could I turn to our other two witnesses? What implications, if any, does extra-territoriality have for your particular sectors?

Lawrence Slade: I agree with what Ashley was saying in terms of national security, but again there is a risk, or you run the risk, of just capturing far too much in the Act as it is currently laid out. The concern is to make sure that only legitimate security concerns are caught in that and that Government focuses on those risks, and not those that will support our need for FDI. If you look in the infrastructure sector overall, the vast majority of assets are owned by long-term patient capital, by pension funds, and so on, who certainly do not pose any form of security risk.

Again, the issue is capturing too many potential deals. Someone asked whether we are building up the bureaucracy again, and that is a potential here because deals need to happen quickly. The more complex we make

the deal process, the more pause for thought investors are given in terms of the UK as an FDI location.

Camilla de Coverly Veale: I was only going to contribute that the UK has traditionally been seen as one of the most attractive markets to launch new and innovative products, so our status as a first-tier country for new services is potentially threatened by the expansive territorial approach.

Chair: At this stage, I am going to hand over to Mr Mark Garnier to chair the remainder of the session. I am greatly indebted to you, Mr Garnier, one of the less obvious wings of the SNP. In seriousness, I am very grateful. Thank you very much.

[Mark Garnier took the Chair]

Q42 **Chair:** Not at all, Angus. Have a very safe flight. You can count on me as being a Unionist in deep cover within the SNP.

Lawrence Slade, your association has suggested that the new regime could be streamlined by means of exemptions for institutional investors with a strong track record of responsible investment in UK infrastructure assets. It sounds like a very good idea, but how would it work in practice?

Lawrence Slade: The first part of it is to emphasise my previous answer in terms of the nature of a lot of the funds that are investing in UK infrastructure. Our research indicates that about 8.5 million UK pensioners have holdings in UK infrastructure. Of course, a lot of those investments are in very regulated markets, whether that be water, energy or comms, for example, where Ofwat, Ofgem and Ofcom have strong regulatory control over those markets, the investments and the actions of asset owners and investors in those sectors.

Using a combination of regulated markets and taking the style and type of investor and their approach to investing—that is, they are not private equity businesses, they are long-term, patient capital looking at deals worth billions of pounds over five, 10, 15, 50 years even—they are not there to make a quick buck, if I can use that colloquialism. They are there to provide stable, steady investment into the UK economy to improve our infrastructure, to invest in issues such as achieving net zero by investing in clean technology. These are partners that the UK wants and they are companies that our FDI regime should look at attracting. Understand the companies that are investing in infrastructure and work with that.

Q43 **Chair:** Can I just be clear about that? You talk about funds, and then you talk about attracting FDI. For example, one of the Robeco pension funds investing in UK infrastructure is a big Rotterdam-based investment manager, and it is a passive investment. It will obviously take an interest, but it is not necessarily going to walk off with intellectual assets from its investment. That is fine, but there are all sorts of other investors

that are coming into these types of things. Are you talking, in what you have suggested, about these big institutional investing houses as opposed to direct investors? You would not include direct investors in what you are suggesting at all?

Lawrence Slade: Many pension funds are increasingly direct investors, of course. The big Canadian pension funds—

Chair: Sorry, you misunderstand. Rather than the collective investment funds, like a pension fund, investment trust or unit trust, that type of thing, do you envisage what you are talking about referring to, for example, SoftBank, which could be making investments in either listed or unlisted?

Lawrence Slade: From my perspective, we do not cover companies like SoftBank. We only work with general partners, local partners and pension funds, et cetera.

Dr Lenihan: This is an idea that the UK wants to keep under review, especially eventually creating exceptions from the notification regimes for certain trusted investors from the UK, domestic investors. As I said earlier, the Act's application to domestic investors makes it far broader than regimes in other countries and I think that is where a lot of the volume is going to come from.

It may also wish to keep under review the possibility of exemptions for trusted investors from what you might call a white list of closely allied and highly trusted countries. There are a couple of caveats to that that are important. The first is that there is nothing magical about being an institutional investor. It is a really broad category. When it comes to protecting national security, even the most responsible institutional investor can make mistakes or pose a concern in certain instances. SoftBank, for example, with Arm, doing a joint venture as it did, did pose some concerns later that I think need to be recognised.

It is important that exemptions never apply to the Secretary of State's call-in power, because there is a favourite strategy of some countries to evade regulatory requirements by setting up a subsidiary in a friendly country or by making an acquisition through something that looks like an institutional investor.

Secondly, to give some context on white lists, they are most often found in EU countries that use lower ownership thresholds for the review of investments made by EU investors or nationals. They are usually used in their cross-sectoral regimes. In the US, FIRRMA created a white list to exempt certain qualifying investors from particular countries in its new mandatory notification process, but that was highly limited to just a couple of types of transactions and it was only given to very particular investors in the UK, Australia and Canada. Even that is under review every two years.

My point is that if the UK finds itself receiving a really high volume of mandatory filings from friendly country investors that turn out to be really low risk, a white list can help, especially by making its own resident nationals exempt from that mandatory filing. But as in the EU and the US, you have to limit those exemptions to specific types of transactions where acquisitions from close allies or trusted investors are less likely to pose a concern. You can really only do that once the regime and the review process are institutionalised and established in the country.

You need to give a chance for the Investment Scrutiny Unit to get its head around all these things, because it is difficult to identify who is the beneficial owner of a particular asset or acquirer, and that is a very high learning curve at the beginning. They need to be given a chance to do that and then the issuing should be kept under review.

Chair: Fantastic. Camilla, how about your sector?

Camilla de Coverly Veale: Yes, we called for a white list and we think it would be incredibly beneficial, especially given, for example, VC funds. Typically, VC funds will have the same investors, the same money, for the lifecycle of the fund, so we think there should be some way of having a pre-approval process they can go through and then every transaction is white listed.

Q44 **Mark Menzies:** Lawrence, your association says that the Government's call-in powers under the Act should be used "sparingly and only in extreme cases". What sorts of cases would count as "extreme" in this context?

Lawrence Slade: It comes down to the extent that there are genuine concerns about security, as opposed to less-tangible concerns about the ownership of a strategic asset by a particular country or in a particular sector. If you think about it, most infrastructure assets do not pose national security challenges and the vast majority of investors, as I said earlier, are well-established investors from friendly countries, which brings that much-valued foreign direct investment in the UK.

The combination of work, as was mentioned earlier, from the establishment of the Office for Investment to make the UK an attractive location is paying dividends and there is a lot to be said for having early communication between potential investors and the Government in terms of whether a particular deal will be called in or not. It goes back to how well you can manage that engagement, how well the team at the Office for Investment and the BEIS team are working together across Government so that, from an investor point of view, you can get a very quick, swift answer in terms of whether you will be called in or not. Then if it is called in, it happens quickly and efficiently.

One quick last point, and we have not mentioned this yet today. Understanding the reasoning behind a decision is absolutely critical from an investor's point of view over time. If I might be indulged for one

second, on the issue of seeing how it goes, develops and evolves, yes, fine, but I still have significant concerns about the volume of deals that could be called in and, therefore, whether the Government can get enough skilled senior people who understand investments involved in the unit in BEIS to get the deals through quickly.

Q45 **Mark Menzies:** Dr Lenihan, what evidence is there about how other Governments use such discretionary powers?

Dr Lenihan: Call-in powers or outreach powers, or whatever you want to call them, are designed as a catch-all to ensure that a Secretary of State or a head of state can protect national security when an investment of significant concern is not captured by that mandatory or voluntary notification system for whatever reason. It might be because the parties involved have tried to evade it, it might be by accident or it might be because nobody realised the issue in time.

That is a really crucial power because it does happen in other countries; it has happened in other countries. I have spoken about that in other Committees; for example, the case of 3Leaf in the US, where you had a Chinese investor purchasing the bankrupt assets of a company that had provided services to the Department of Defense. It was only caught much later because a member of the feed-in system to CFIUS happened to be looking on LinkedIn and saw that the former CEO of 3Leaf was now working for Huawei.

These things do happen. The call-in power is important. Traditionally, that outreach power is used sparingly in other countries like the US where non-notified covered transactions posing that kind of concern have been fairly rare. But as the number, scope and complexity of covered transactions increase, so too are we likely to see the use of this call-in power.

Again, we have to trust Government a little bit in the sense that we want to ensure that the Investment Scrutiny Unit and the Secretary of State have the discretion to use this power when they need to. But as the previous witness just said, they need the support behind them to handle the volume of cases that they are going to have.

There are a lot of countries now, to give you an example, that are trying to track down investments that they have missed in the past because they were underresourced, because of the volume not just of cases that are captured under the regime but in the volume of strategically motivated investments that are increasingly happening across the world. This is not just coming from one country, this is coming from many countries.

CFIUS, for example, created a SWAT team to track down—this goes back to the point about venture capitalists—particular instances where venture capitalists in the tech sector had Chinese or Russian funding that had turned out to be issues of concern. This is a new area that it is looking at

because it turned out that it was an area of new risk transfer that it had not realised was occurring.

France has a new unit like this. It is called the Strategic Information and Economic Security Service. It draws on a nationwide network to try to understand when these transactions happen. So it is important. Yes, it should be used sparingly; yes, it has been used sparingly in the past. It is the emergency system, it is the emergency brake on the Bill, if you will.

Mark Menzies: That is very useful, thank you.

Q46 **Anthony Mangnall:** Very quickly and simply, and I will throw this open to the floor, how much of a risk is it that this process could be politicised?

Camilla de Coverly Veale: Simply because it was in our evidence, I am happy to talk about it. I think it is highly likely that the process will become politicised, simply because the Secretary of State is given a broad range of powers and broad discretion to interpret and use those powers as he or she sees fit, with very little oversight. Coupled with a very loose definition of national security, we are very worried that even though the current Government are very focused on preserving the focus on national security, that is not to say that a future Government or a future Secretary of State could not be swayed by an intense lobbying campaign or a media campaign or something.

To quickly conclude, we think there is a very legitimate debate to have about the national interest and how Government preserves or protects the national interest, but we think that debate should be out in the open and not through the back door of a piece of national security legislation.

Q47 **Anthony Mangnall:** Do you have any suggestions as to what it should look like to stop it being politicised?

Camilla de Coverly Veale: The big question. Anything we can do to help depoliticise the issue and give more oversight would be helpful.

Anthony Mangnall: If you are advocating greater parliamentary scrutiny, I think you will have no fight from any of the MPs on this Committee.

Lawrence Slade: Very quickly, I touched on the transparency point earlier. That is critical in this regard. Also, very clear published criteria against which deals will be called in can form part of that. Concentrate on transparency, clear criteria and, yes, parliamentary scrutiny if things are not seen to be going correctly.

Anthony Mangnall: Good to hear, thank you.

Dr Lenihan: A couple of things. First of all, I agree greatly that transparency is needed. Proportionality of response needs to be proved over time. In the regulations there should be clear guidance given to investors about the types of national security concerns that will be looked

at in this risk assessment process. Those are all things that countries that do this well do.

If you look at the entire OECD and a number of other countries that have these types of regimes, those that are as transparent as they can be, they are proportionate in their response and provide some guidance about what national security means—but not a definition, because you cannot define it.

Q48 **Anthony Mangnall:** Forgive my ignorance, but who do you rank as the best in the world in terms of getting this right?

Dr Lenihan: The US system is the second oldest, technically. It is the oldest in its current form. CFIUS has been around since the 1970s but there have been different forms of this legislation in the US since World War I. It does a very good job at getting things right—and this is something that I have said repeatedly in other forums—because it has a multiagency feed-in process. It is a way of ensuring that the process does not become politicised. It is a way of ensuring that different voices are heard about what the meaning of national security is. It helps things pass the judicial review process later.

Because it is such an institutionalised process and because it goes across Government and across sectors, and provides investors with very detailed regulations and examples, it still has the highest level of foreign investment in the world, despite having, before this, the most comprehensive review regime under law in the world. It has done a good job.

Q49 **Anthony Mangnall:** To cut through on that, we should not be afraid of having a comprehensive system that may have high levels of regulation and bureaucracy, because ultimately, if the attraction is there, people will win through. They will still want to be able to come and invest and do what they do.

Dr Lenihan: Yes, you do not want bureaucracy or red tape behind this. What you want is multiagency feed-in to the Investment Scrutiny Unit from across Government, the Foreign, Commonwealth and Development Office, the Home Office, the MoD, the Department for International Trade, GCHQ. You want them all to help in the risk assessment process because they have things to offer. You want them to help in the monitoring process because they can help reduce the burden of that caseload, and because they offer a different set of voices that are important to have in that conversation so that the Secretary of State has a balanced view and opinion coming to him before he makes a decision.

Anthony Mangnall: You are all very on message, which is becoming extremely helpful in terms of formulating a view on this. I am conscious of time, but thank you. Those are three incredibly helpful answers, from my perspective anyway.

Q50 **Chair:** Ashley, to pick you up on that last point about the feed-in from all

the different Departments, what you described already operates with the Export Control Joint Unit looking at the export licensing regime. Do you think ECJU should have more of a role to play in all this?

Dr Lenihan: I definitely think it should be part of the feed-in process. It is very hard for us, from the outside, to know right now what the Investment Scrutiny Unit is going to look like. We know its funding, we know it is going to have 100 people and we know it is going to sit in BEIS, but we do not know yet who is contributing and how. One would think that you would want seconded staff with training and with security clearances from a host of Government Departments, including the unit that you just mentioned.

Q51 **Chair:** The reason I mention it is that the ECJU is already doing it, because ECJU works, obviously, within DIT but it has International Development, MoD, Foreign and Commonwealth Office. The only bit we need to add into this in order to make it the scrutiny department would be BEIS, and you already have an up-and-running model. Have the Government got this wrong? Maybe that is a thought question.

Dr Lenihan: I will say other western countries, especially in the EU, the US and Australasia, tend to keep these regimes in either a Treasury, Trade or Finance Ministry and have other Ministries feed in. The reason for that is probably to allow for some consideration of broader strategic concerns rather than simply just the technological concern that might be attached to certain transactions. I am not talking about the political football that we were earlier. There are broader strategic concerns that at the highest levels of Government can sometimes get lost in some of those units. You need to have a combination of both.

Q52 **Mark Menzies:** This is to all panellists. DIT says that the Government's approach to investment screening is "actor agnostic", taking a case-by-case approach to individual assets and companies without preconceptions. What case might there be for focusing attention on certain particular countries or investment bodies, thinking particularly of sovereign wealth funds? Camilla, let's start with you.

Camilla de Coverly Veale: I am not entirely sure whether I am the best person to ask this or to have much of an interesting comment. The only thing I will say is that, obviously, the case of Imagination Technologies has loomed large over this debate, so I am not sure that focusing on where something has headquarters is necessarily the most important factor.

Mark Menzies: Thank you for your honesty and brevity.

Dr Lenihan: At the end of the day, even if you know that there are actors with intent to do certain things in certain sectors, whoever they might be and wherever they might be located because of certain stated Government policies, the reason behind being actor agnostic is that it can be difficult to tell who the ultimate owners of some of these investment vehicles are at the outset. It is important not to assume that you know

who the ultimate owners are until you have done your investigation. As I said, that is one of my concerns about ensuring that this future regime is well staffed and has the capacity behind it to be able to go properly into that and handle the necessary volume of cases.

That being said, most FDI regimes based on national security, western or not—the Chinese and Russians do this as well—recognise that state-owned, influenced and operated entities potentially pose more of a risk to national security than others by the logic that they are strategic in nature and they are beholden to that state's Government and that Government's laws.

Most regimes, whether in practice or in regulation, tend to screen state-owned, financed and influenced entities more than others. In the special case of sovereign wealth funds or state-operated pension funds, yes, most are market actors with proven track records of independence. I completely agree with that, but it is not true in every case. There are sovereign wealth funds with proven track records that will sail through the review process. That is the idea, that those ones sail through.

It is strange to know that we flag such state-owned entities, because there are equally many cases of sovereign wealth funds that act in strategic ways. The Norwegian pension fund acts in strategic ways. China's sovereign wealth funds are not only strategic in their investments but they are also financially supportive to other investors and strategic investors that are subject to the national security law in that country.

As I said, even the sovereign wealth funds of our allies make strategic investments to support their national champions, like the French, or to encourage the growth of the domestic tech or aerospace sectors, like sovereign wealth funds in the Middle East do. Again, while most investments are going to be found to be benign from that kind of actor, that is okay because they will go through the process quickly. But it would be a mistake not to look at them, at least in practice, a little more carefully.

Mark Menzies: That is very useful. You never know, we might end up doing a future inquiry into this. Let's watch this space.

Lawrence Slade: Obviously, I cannot talk for all sovereign wealth funds, but in our experience even sovereign wealth funds tend to have a fairly significant amount of autonomy in terms of how they operate and how they invest. Frankly, most if not all funds will act strategically in some manner, shape or form, whether they are UK owned and operated or not, so I might take a little bit of issue with Ashley there.

Do not forget that, from an infrastructure point of view, the vast majority of assets are in regulated sectors. It is not just the Government looking at this from an FDI point of view; it is also the regulators in those sectors looking at how those companies, those assets, are operated, to ensure that they are operated in the interests of the society that they serve.

Q53 **Chair:** I have one last question, Lawrence. How much is known about the role that the Department for International Trade is going to be playing in the new regime? Following on from the question I was asking earlier of Ashley, what role do you think it ought to play?

Lawrence Slade: The Office for Investment and the Department for International Trade have a crucial part to play here, and not just in terms of conversations with investors thinking about coming to invest in the UK. The co-ordination part across Government has been mentioned a few times this afternoon, and making sure investors understand which Government Departments they are going to be talking to or will need to talk to, what the questions might be and what the issues might be.

The Office for Investment can and should be absolutely central to that. Gerry Grimstone and his team need to be very much engaged with the BEIS team, and I know he has a foot in various camps. That co-ordinating role across Government will be a critical part of making this process work. So, yes, very, very important.

Q54 **Chair:** You mention Gerry Grimstone's double-hatting. He is Minister of Investment in DIT and BEIS. Do you think that is good enough? Does that bring the two together?

Lawrence Slade: We can all, I am sure, over the years look at examples where Government have not been joined up enough. The challenge for the Minister, Lord Grimstone, and his colleagues will be to ensure that there is this streamlined connectivity across Government so we can get the decisions that are needed for investors and for consortia put in place quickly and efficiently.

We all know that bidding for an asset, bidding for a project, is not just paperwork. It has a cost in the tens of millions sometimes, so the more efficiently the Government can run this process, the more likely it is that investors are going to be attracted to, or will continue to be attracted to, the UK as an investment centre and home.

Camilla de Coverly Veale: We are very worried that one hand of the Government may be doing something while the other hand is not. We fear the risk that the Office for Investment might help a tech start-up gain a particular foreign investment, and then it goes to the BEIS unit and the BEIS unit says no. As long as that messaging can be clear and consistent across Government, we would be very happy.

Q55 **Chair:** You raise an interesting point about the ECJU. The Department for International Trade will be promoting exports from certain companies to certain countries. If it turns out the ECJU will not then grant a licence under the consolidate criteria, that seems a particularly peculiar sort of approach. Ashley, do you have any final comments on any of this?

Dr Lenihan: First to reiterate the basic, which is that if you have regularised feed-in from multiple agencies, you are less likely to be

politicised and more likely to withstand judicial review and get through the assessment process.

DIT, along with other agencies, could play a crucial role here in potentially raising the flag on potential trigger events that might not necessarily appear on the Government's radar through the monitoring of traditional databases and repositories. I do not think you can overestimate the importance of built-in redundancy in that process for capturing spurious investments for call-in and review.

Like the Foreign Office, I think DIT also, because of its extensive foreign networks and knowledge of foreign actors, should be properly utilised to help raise those red flags but also to help say that a particular investor is okay. That is because it has the knowledge of national trade and investment strategies and policies, it can provide context behind a trigger-event risk, it can provide context behind certain targets and acquirers as well. In particular, there is a knowledge in DIT of the laws of the acquirers' home countries in a number of cases that can be particularly useful, whether they are around anything from nationalisation of property to Government demands for information. That can be helpful.

The role of DIT is clear. The role of the Office for Investment is a little less clear at this particular moment because it is a new Department, but I think it can offer knowledge of certain investors. Because it is the Department tasked with fostering foreign investment into the UK, its optimal role would be that hand-holding process of helping investors navigate the new regime. It might be perceived that there is a bit of a conflict of interest if it were involved in the assessment process, but in terms of helping investors navigate the regime, know who to contact, as the other witnesses said, know where to go, know what numbers to call, that could be a really helpful role for helping to foster investment over the long term.

In other countries that have done this well, the number of who to call and who to talk to is very clear and it is made clear over time. Where countries get into trouble is when investors do not know how to do that, so that would be a good role for them.

Chair: Fantastic. Thank you all very much indeed, Lawrence Slade, Dr Ashley Lenihan and Camilla de Coverly Veale. Thank you all for coming in.

We have run slightly over time, about 20 minutes, but we have come to an end. Thank you to all the teams who have been asking questions.