Linklaters

First-ever appeal against an NSIA unwinding order: will the judiciary exercise its oversight over matters of national security?

28 November 2024 Anna Mitchell - Mark Daniel - Erasmia Petousi ForeignInvestmentLinks

Since the introduction of the National Security & Investment Act 2021 (NSIA) there has been significant speculation as to the level of judicial oversight that English courts would be willing to exercise over the UK Government's national security decision-making. Now, with the High Court's recent judgment in LetterOne's appeal over the Government's order to divest its completed purchase of Upp, we have the first indication of how the courts will exercise that oversight. This post explores the key learnings from this decision and whether any deference shown to the UK Government is likely to be a blueprint for future NSIA appeals.

A quick reminder of the facts

In January 2021 (a year before the NSIA came into force), investment company LetterOne acquired the entire share capital of Upp, a UK broadband provider (altnet). LetterOne is ultimately owned by a number of Russian nationals, four of whom were designated as sanctioned persons following Russia's invasion in Ukraine in February 2022.

In May 2022, the Investment Security Unit (ISU) issued a call-in notice in relation to the transaction. In written representations to the Secretary of State, LetterOne indicated that two of the sanctioned owners, Mr Khan and Mr Kuzmichev, had sold their shares to a nominee company whose Ultimate Beneficial Owner (UBO) was Mr Kosogov (not being subject to sanctions). The only UBOs within the LetterOne group subject to UK sanctions were Mr Fridman and Mr Aven, and measures had been put in place to ensure they would not be involved in the day-to-day running of Upp. Remedies negotiations were not successful, and LetterOne's wish to retain some limited representation on Upp's board of directors was rejected by the Secretary of State, who ultimately ordered the divestment of Upp. LetterOne challenged this decision by judicial review in the High Court.

Key learning 1: a significant margin of appreciation will be afforded to the Secretary of State in assessing national security matters

While central to the operation of the NSIA, the concept of national security remains intentionally undefined in legislation. This has been a point of contention in the parliamentary debates surrounding the NSIA, and the explicit recognition that national security must remain a fluid concept affords decision-makers a significant margin of discretion.

The High Court's judgment reaffirms this flexibility of the executive, acknowledging that "*the court will treat as axiomatic that Parliament has entrusted the assessment of risk to national security to the executive and not to the judiciary*". Decisions on the national security risk of a transaction involve matters of judgement and policy, and the courts may be unwilling to second-guess the judgement of the executive on such matters.

This is a recurring theme in the judgment, reflected in how the court approaches both (i) what the executive perceives to be a national security risk and (ii) the assessment of proportionality of the intervention to counter that risk. At the first level, the claimants' attempt to "reframe" the national security risk presented in the case was characterised as "*impermissibly narrow*", with the court noting that it failed to encapsulate "*the breadth of the risk on which the Secretary of State is entitled to rely*". At the second level, the court expressly acknowledges that the Secretary of State "*is the constitutional decision-maker*" and thus the court "*should give weight to the Secretary of State's view of the balance between competing rights and interests*". Considering that "*the vital importance of the community's interest in national security must be given considerable weight*", the judgment strongly affirms that the court's "*lack of institutional ability to make its own predictions about the future warrants a high degree of judicial restraint*".

Key learning 2: expect limited disclosure

As part of its appeal, LetterOne claimed that during the NSIA review, it was given insufficient information about the risks to national security that the ISU was exploring, or the remedies under consideration to allow it to make meaningful representations. However, the court was not swayed by these arguments. Whilst it acknowledged that the claimants could have been provided with more information during the administrative process, it noted that while the "*call-in notice was unenlightening*" the parties were informed "*of the gist of the national security risks*". According to the court, it is not enough for the claimants to say that the decision-making procedure could have been better. They must "*show that the procedure is actually unfair*." In that respect, the court noted that the Secretary of State enjoys a very broad discretion to choose how to make its decisions and can decide when to make any disclosures, bearing in mind the need for finality in decision-making. In summary, the ruling indicates a high threshold for potential claimants seeking to advance an "unfair procedure" ground of appeal.

Key learning 3: other statutory powers may not get traction within the NSIA context

The claimants were also unsuccessful in their attempt to show that the Secretary of State had failed to consider other relevant statutory powers that would have provided them with additional avenues falling short of unwinding. The court explored these avenues for completeness, but its position was unequivocal that in the context of national security, "*where constitutional boundaries should be respected and clearly drawn, the selection of statutory power by the Secretary of State – rather than the lawfulness of its exercise – was either non-justiciable or on the cusp of being so*". The judgment expresses a clear position that decisions on national security are almost outside the purview of judicial oversight – even within the already narrow confines of judicial review.

Key learning 4: proportionality is a challenging argument

The claimants' third ground of appeal was based on the infringement of the right to the peaceful enjoyment of property set out in Article 1 Protocol 1 of the European Convention of Human Rights (A1P1). The court was sympathetic to the claimants' argument that, in this case, the degree of state involvement in overseeing and monitoring the sale of Upp's shares under the stringent terms of the order brought the practical difference between a de facto expropriation (under para 1 of A1P1) and control of use (under para 2) to "*near vanishing point*". That said, however, the legal test of proportionality to be applied remains the same.

In this respect, turning to the question of fair balance between the general interests of the community and the individual rights of the claimants, the court again deferred to the Secretary of State's discretion, noting:

i. the "*vital importance of the community's interest in national security*";

ii. the multifactorial assessment of risk to national security, which "*warrants a high degree of judicial restraint*"; and

iii. the fact that proportionality is part of the legal test for making a final order (which the court seems to take as equating to this test having been part of the Secretary of State's assessment).

The question of less restrictive measures was dealt with in similar terms, with the court remaining unpersuaded that those argued by the claimants - including keeping all "*critical physical network assets*" in the UK, restrictions on board appointments and limits on information sharing - would have attained the same objective.

What does the decision mean for the direction of travel?

Whilst the outcome of the judgment is unsurprising, the decision recognises a very broad discretion to the UK Government across the board, in terms of substance as well as process. This indicates a high evidentiary burden for potential claimants appealing an order made under the NSIA.

For instance, LetterOne's suggestion that the final order was driven by diplomatic rather than national security grounds was rejected merely on the basis that "*a fair reading of the documents before the Secretary of State does not lead to the conclusion that the Order was imposed for reasons other than national security*". The court also sided with the UK Government, effectively agreeing that Mr Fridman and Mr Aven stepping down from LetterOne's board and having their shareholdings frozen was not sufficient as a remedy.

Does this mean that significant deference to the UK Government's decision-making can be expected? Though it is too early to tell with certainty, the UK's first court decision indicates that claimants will have an uphill struggle to persuade UK courts that a final order fails the test of judicial review. Given that the ISU has been criticised by certain stakeholders for the opacity of its decision-making, the court's dismissal of the claim that the process is procedurally unfair will also be welcomed by UK Government. Despite the high legal hurdles, however, there may nonetheless be good commercial reasons for investors to pursue challenges - even if they are ultimately unsuccessful and the decision is not overturned, claimants may still be able to benefit in terms of accessing additional information through the disclosure process in the courts.