Law Council
OF AUSTRALIA
Business Law Section

Manager
International Investment & Trade Unit
Foreign Investment & Trade Policy Division
Markets Group
The Treasury
Langton Crescent
PARKES ACT 2600
Via email: ForeignInvestmentConsultation@treasury.gov.au 20 March 2015

Dear Sir or Madam,

Attached is a submission which has been prepared by the Foreign Investment Committee of the Business Law Section of the Law Council of Australia ('the Committee'). The submission is in response to the Federal Government's Consultation Paper on Strengthening the Foreign Investment Framework.

Members of the Committee would be pleased to participate in further discussions with representatives of the Treasury.

In the first instance, please contact the Committee Chair, Malcolm Brennan, on 02-6217 6054 or vial email: malcolm.brennan@au.kwm.com

Yours faithfully,

John Keeves, Chairman
Business Law Section

enc.

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ATTACHMENT A — CONSOLIDATED CONSULTATION QUESTIONS

THE FOREIGN INVESTMENT COMMITTEE OF THE BUSINESS LAW SECTION OF THE LAW COUNCIL OF AUSTRALIA MAKES THIS SUBMISSION IN RESPONSE TO THE GOVERNMENT'S CONSULTATION PAPER ON STRENGTHENING THE FOREIGN INVESTMENT FRAMEWORK.

It is strongly submitted that the proposals suggested in the options paper be carefully considered and that proper time be allowed for implementation and that changes are not rushed. Irreparable damage to Australia is inevitable if measures are inadvertently put in place that deter investment, in particular from the very sectors in which the Government is attempting to promote investment. There is a significant risk that will occur if extensive or complex changes of the kind proposed are effected without proper consultation and careful testing of proposed amendments.

NEW COMPLIANCE AND ENFORCEMENT AREA IN THE AUSTRALIAN TAXATION OFFICE

1. **The government seeks feedback on the creation of a new compliance and enforcement area in the Australian Taxation Office:**

   - *Has the Government investigated whether the ATO will be able to perform the function effectively given its background is in tax administration, not reviewing compliance with Australia's foreign investment regime?*

   - *In particular the Committee expresses concern that if the ATO is in charge of compliance and enforcement with respect to foreign investment, then that sits uncomfortably and may in some cases create tensions with their existing obligations to effect compliance and enforcement with existing taxation revenue laws, and any proposed taxation laws. ATO expertise is in relation to compliance with revenue laws, and not with the policies and laws relating to foreign investment generally.*

   - *The Taxation Committee of the Business Law Section of the Law Council of Australia has previously made a submission to the ATO in relation to the non-final withholding tax on transactions involving taxable Australian property. A copy of that paper can be found at the website www.lawcouncil.asn.au/lawcouncil/index.php/library/submissions (the WHT paper). The Committee reminds Government of the recommendations contained in the WHT paper, noting that there are a number of overlaps with the current consultation.*

   - *The WHT Paper echoes comments in this paper relating to the shifting or imposition of liability on the legal profession by making practitioners personally accountable for responsibilities of their clients through an enhanced penalty regime, as well as the difficulty of categorising and defining different items of land and of taxable Australian property.*

   - *The Committee (as the Taxation Committee did in the earlier consultation) is concerned that some of the proposed changes create the imposition of red tape, complexity and compliance burdens.*

- *Information sharing controls will need to be properly established if this function is performed by the ATO. Confidentiality and the protection of privacy concerns are important to the integrity of the regime. The ATO comes into possession of data in various capacities. It also comes into possession data via exchange of information arrangements with State and other investigative bodies. There is therefore a need to legislate how data gathered for one purpose is quarantined unless legitimately able to be used for another purpose. For a formal compliance and enforcement function, existing arrangements may need to be made more robust than current information sharing arrangements. Legislative amendments and/or Memoranda of Understanding between Treasury, the ATO and State Land Titles Offices should be considered. The ATO would also need to develop protocols for internal team use of information.*

a. **Is the creation of a new compliance and enforcement area required to address concerns with foreign investment framework compliance?**

- *It is obviously appropriate that Australia's foreign investment laws be enforced.*

- *However, there appears to be a lack of substantiated data establishing that a new compliance and enforcement area is actually required. Revenue could be better directed towards an educative and/or a monitoring function as an initial step to establish whether or not there is a need for a dedicated compliance and enforcement area.*

- *Outside the residential real estate area, in our view there has generally been a strong culture of compliance, and of law firms advising compliance (including compliance with Policy which is not mandated by statute, and in areas where there is doubt as to how the statute applies), as well as effective oversight by FIRB which has led to queries/rectification in instances of non-compliance. It is unclear why this position needs to change, particularly as the establishment of a new compliance and enforcement area is likely to be costly, and could lead to inconsistent enforcement approaches.*

i. **Are there alternative approaches that should be considered?**

- *Commit revenue to an educative and/or monitoring function as an initial step to establish whether there is a need for a dedicated compliance function before committing revenue to a full compliance and enforcement area.*

- *If a compliance and enforcement function is ultimately considered necessary, the function should preferably be performed within FIRB. FIRB understands and deals with the regime on a daily basis. There could be a disconnect between understanding the regime and the practical application of the regime if another Government body were to exercise the function. It would also seem desirable to connect the charging of fees to the relevant educative/monitoring functions and/ or compliance/enforcement functions of FIRB within Treasury. We*

appreciate that improvements to current resourcing and training would be required to establish this function within the FIRB.

INTRODUCING FEES ON FOREIGN INVESTMENT APPLICATIONS

2. **The government seeks feedback on the introduction of fees on foreign investment applications, including:**

   a. **Should the Government charge application fees on foreign investors to fund screening, compliance and enforcement activities?**

   - *It is not clear what the justification for charging fees on business applications is, as there has never been a concern about avoidance of notification obligations in relation to commercial real estate investment or business investment transactions which would justify an increase in screening, compliance or enforcement activities.*

   - *There is no justification for charging an application fee for business applications or commercial real estate investment where that fee will be used to fund a compliance and enforcement function directed at residential real estate investment (and rural investment). Only a fee imposed on residential real estate applications (and rural land applications) can be justified as funding for enforcement functions directed at those activities. If a fee is to be applied, it should be directed at funding improved resourcing of FIRB's investment review function and to initiatives to encourage foreign investment, not to functions that are not related to business investment.*

   - *We also believe serious consideration should be given to limiting the fees to residential real estate applications. We recognise that there is a level of popular concern that foreign purchasers compete with Australian home buyers for Australian housing stock and that (whether or not one agrees with this perspective) imposition of fees on residential real estate applications may be welcomed by some sections of the community who are concerned by this. However, business investment in other sectors (for example in resources and infrastructure) has been overwhelmingly positive for Australia and should not be discouraged. Australia is not the only possible destination for these investments funds, and we will be seriously disadvantaged if these funds go elsewhere.*

   - *The proposed fee structure for investments in rural land is too high and would be an active disincentive to investment in the agricultural space. This is contrary to the government's stated aim of attracting investment in the rural sector. The proposed fee scale fails to recognise that rural land operations are commercial agribusinesses. There is different treatment of rural land acquisition and agribusiness acquisition – for example a $1 billion agribusiness proposal has a $100,000 fee, yet that same fee is payable for a $10 million farm.*

   - *The proposed fees coupled with stamp duty costs start to make the cost of investing in Australia uncompetitive.*

- *Charging a fee puts Australia at a comparative disadvantage to other countries such as the United States, Canada, Japan (to name a few), particularly in the context of business applications and commercial real estate applications. The options paper also fails to examine other countries that compete for foreign investment (e.g. China, Russia, Brazil, UK, Ireland, Mexico, Spain, Germany to name a few).*

- *The proposed fees are of such a size that they have potential to distort the market. The fees will have an impact on the shaping of transactions.*

- *If fees are to be imposed they should be used not just to fund compliance and enforcement activities but also better resourcing of FIRB so that FIRB is able to provide a better service - deal with notifications more efficiently (especially the overwhelming majority of business notifications that are cleared), improve transparency and predictability through improved guidance and facilitate investment transactions such as by offering fast-track clearance for urgent cases. Increased fees for urgent applications would not be objectionable.*

i. **Are there alternative approaches that should be considered?**

- *Impose a fee on residential real estate applications but not commercial real estate or business applications.*

- *Impose smaller fees.*

- *The proposed agriculture fees should not include the incremental fee for rural land acquisitions. The agribusiness category could then include all rural land acquisitions of more than $1 million.*

ii. **Should there be any exceptions to paying the application fee?**

- *The fee should not be imposed on business or commercial real estate applications. Also see our response to part c. of this question.*

- *A fee should not be required for internal restructures of foreign owned groups*

- *A fee should not be required for offshore foreign to foreign transactions (that is, acquisitions by foreign persons of interests in offshore companies who have Australian subsidiaries or assets).*

- *The fee should not be payable for applications made under the Policy rather than under the Act. In particular, applications by foreign government investors for:*

    (1) acquisitions of interests in land;

    (2) a direct investment in Australia;

  should not be subject to fees unless the application is also required to be made under the Act.

At present, all such investments are required to be notified regardless of the value of the investment. This A$0 threshold is extremely low by international standards and the definition of a foreign government investor is defined broadly. To charge fees for such applications would be inappropriate and would act as an impediment to foreign investment by such entities.

- *If fees are imposed mechanisms should be available to provide flexibility, such as the conferral of a discretion on FIRB or the Treasurer to waive all or part of a fee in certain circumstances, or classes of circumstances. The examples given above are just a few instances of circumstances that would justify a waiver or reduction of fees and others are likely to come to light. Without flexibility there will be increasing frustration with the screening process and increased risk of non-compliance. There should be a commitment to review the fee structure within a short time following its introduction (such as 12 months).*

- *Where multiple bidders are making applications as part of a competitive sale process, the fee should be deferred and payable only by an applicant that has been identified as the preferred bidder in the sale process. Fees should also be refundable on request if the acquisition the subject of the approval does not proceed. Otherwise bidders at auctions and in other competitive bidding situations may lose substantial sums (more than just a cost of doing business) without securing any transaction.*

b. **Is the level of the fees appropriate?**

- *Is it expected that the anticipated $200 million of fees will all be required to fund the enforcement and compliance function? What will any shortfall/excess be used for?*

- *The fees are higher than those recommended by the House of Representatives Economics Committee. What is the justification for including higher fees than those recommended, and higher than those in other countries?*

- *The fees are too high. A lower fee would be more appropriate and reduce the negative impact the fees may have on foreign investment.*

- *The size of the fees and the impact on regular investors are likely to be a disincentive to invest in Australia, particularly in the business and commercial real estate sectors where foreign investment substantially benefits the Australian economy.*

- *Further consideration should be given to the fee schedule. It may not be appropriate for the same fee to apply to a purchase of property and leases or licences. Fees should not be payable for incidental acquisitions of land such as easements for pipelines and licences or leases to install telecommunications equipment. The fee schedule proposed seems to*

assume that all land acquisitions will involve the purchase of real estate. This is not the case. Consideration should also be given to the fees for annual programmes.

- *Also see our response to part a.ii of this question.*

i. **Will the fees act as a barrier to foreign investment?**

- *In many cases yes.*
- *The fees may send a signal that Australia is not open to foreign direct investment.*
- *One reason why fees are likely to irritate is that there is not a clear enough connection made between the fees being charged and the purpose or use made of the fees, once levied. Connecting fees charged more directly to the FIRB functions of education and monitoring and/or compliance and enforcement would seem more coherent. The level of fees proposed goes considerably beyond that which would be required by a pure cost recovery model.*
- *It would also be desirable to ensure that, if (contrary to this submission) fees are charged on business or commercial real estate applications, they are not diverted to pay for residential real estate enforcement.*
- *The fees may decrease Australia's comparative advantage if opportunities with similar rates of return on investments are available in countries with no fees.*
- *Although the fees may not represent a large proportion of the overall value of a transaction, they add to the final price and could make or break decisions to invest. Fees will create an imbalance in the competitive process between foreign and domestic organisations.*
- *As the fee will apply even where the property or business is not eventually purchased, this may act as a disincentive to consider investing in the first place.*
- *What other countries are charging fees (NZ, Singapore, Hong Kong, others?) and how do they compare with the proposed fees? Do they charge fees for business or commercial real estate applications? What has been the experience with charging fees in those countries?*
- *If fees are levied, they should be based on the funds to be invested rather than the value of the underlying gross assets. A fee based on the value of the target's gross assets assumes that a 100% interest in the target's assets is to be acquired and that the target is not geared. For example, all investments in urban land corporations and urban land trusts need to be notified and the value of the gross assets may not bear any correlation to the amount invested due to*

the level of gearing within an entity. Any fee levied should be based on the dollar value of the investment. It would be inherently unfair for the acquirer of a 1% interest in an entity to pay a fee based on the value of the entity. A flat fee is also not appropriate in these circumstances. The Foreign Investment Policy encourages early contact with the FIRB. The imposition of fess will mean that investors will wait for more certainty on the deal (particularly in bid situations) before contacting FIRB. This will result in more urgent applications. It may also result in a lower level of compliance by those investors who are unaware or uncertain of the breadth of the Policy's requirements (since fees may discourage them from contacting FIRB for clarification).

- *Also see our response to part a.ii of this question*.

ii. **What might be the cumulative impact on business reinvestment?**

- *The fees may discourage repeat investment in Australia by businesses with existing investment in Australia, as the fees add to transaction costs. This may be the case where comparable investments (in terms of rate of return) are available in other countries with lower or no application fees. Certain current investors may make regular applications to FIRB for low level investments, but following the introduction of fee for each application, they may not continue to make that investment.*

- *Straightforward applications will effectively subsidise more controversial applications.*

- *Foreign investors who comply with the law will effectively be forced to pay for enforcement against those who do not. Areas of investment where the former are most prevalent (eg business) will effectively subsidise areas where avoidance is most common (allegedly, residential real estate).*

- *This is very much a question that will depend on the individual investor and availability of investment alternatives elsewhere*.

c. **What options should be considered to ensure applicants that submit multiple applications (for example, bidders at auctions or business applicants that withdraw and resubmit) are not charged excessive fees?**

- *Multiple applications (e.g. bidders at auctions): Only require a single application fee where submitting multiple applications within a certain time period (for example within 6 months).*

- *Withdrawal and resubmission: Only require an application fee for the first submission. Waive the fee where an application is withdrawn and resubmitted.*

- *Payment on success only: charge a 10% application fee on filing with the balance paid only completion of an acquisition.*

- *No upfront fees payable for participation in auctions or competitive tenders. The fee to be payable only upon success.*

- *Particular consideration should be given to foreign government investors in this context, given the zero dollar threshold for applications for such investors.*

- *Consideration should be given to a one-off annual fee for foreign investors and their subsidiaries who make multiple applications (particularly foreign government investors who may have a large number of small dollar value investments given the zero dollar threshold for applications). There is substantial risk that repeat investors faced with significantly high fees will reduce their investment in Australia as a reaction to the higher fees.*

- *Conferral of a discretion on FIRB to allow for the waiver of fees for certain types of application. This would allow for flexibility in the operation of the legislation.*

- *The fee structure and amounts should be provided for in the regulations and there should be mechanisms to provide flexibility such as the conferral of a discretion on FIRB or the Treasurer to waive all or part of a fee in certain circumstances or classes of circumstances. (see section 2a.ii above).*

PENALTY REGIME

3. **The government seeks feedback on the proposed changes to the civil penalty regime, including:**

The current regime of offences and penalties for alleged non-compliance with the foreign investment framework may need to be updated to recognise that changes have occurred since its introduction. However, any increase in penalties, the introduction of a civil penalty regime, or the proposed inclusion of the infringement notice regime into the relevant regulatory framework at this time without further research and assessment by a body such as the ALRC, would be an error, in our view. More research and evaluation of the various alternatives in light of evidence of the failings in the current system should be carried out and carefully considered. We are not aware of any detailed research or experience in FIRB of such material.

Further, when looking at accessorial penalties, the role of a lawyer as trusted adviser may be compromised unless it is clear that the lawyer is only liable for penalty as having assisted the doing of a transaction with actual knowledge that the transaction was in breach of the legislation.

We provide more detailed comments on the penalty regime in the attached short paper.

a. **Would a civil penalty regime be an effective addition to the rules to ensure compliance and assist with enforcement?**

- *There appears to be a lack of substantiated data establishing that a compliance and enforcement area is actually required. This creates the perception that the introduction of a stronger penalty regime is due to political pressures rather than based in evidence.*

- *There is a threshold issue of policy as to whether civil penalties will be an effective answer to the perceived problems. Well-publicised criminal proceedings and divestment might be better approaches to high profile breaches and might be sufficient.*

- *Due to the complexity of the legislation and the Foreign Investment Policy, a number of investors have needed to lodge retrospective applications to ensure they remain compliant with Australia's foreign investment regime. To date, the relationship between investors and FIRB has encouraged the submission of these retrospective applications. Investors should be encouraged to continue to come forward with these retrospective applications, but the introduction of a penalties regime may have the opposite effect.*

- *The options paper discusses penalties on the basis of whether investors would have or wouldn't have received FIRB approval. There can often be a range of views as to the correct application of the Foreign Investment Policy, and penalties may therefore have an anomalous effect.*

- *Revenue could be directed towards monitoring the market to determine the nature and frequency of FIRB non-compliance. This would serve as an initial step to better design a successful penalty and compliance regime.*

- *Will enforcement of penalties be run by the ATO? Is it clear the ATO currently has the capability to enforce such a penalty regime given its background is in tax administration?*

- *The primary issue with non-compliance appears to be the failure of foreign investors to notify FIRB prior to making acquisitions in residential real estate. Through what mechanism will the ATO be able to detect or enforce new penalty regimes? Will the monitoring of land titles be sufficient to detect purchases by foreign nationals?*

- *Information sharing controls will need to be properly established if this function is performed by the ATO. Confidentiality and the protection of privacy are important to the integrity of the regime.*

- *Whilst recognising the deterrent value of penalties, questions remain. How much will enforcing the penalty regime cost and will it be significantly more or less than the amounts paid under the penalty regime? Will the penalty regime be funded primarily from the proposed fees? If so, how much of the anticipated $200m of fees is expected to be used to fund the enforcement and compliance function?*

b. **Are the proposed penalty amounts appropriate and likely to serve as a deterrent?**

- *A penalty rate of 25% of property value is high. It is not clear whether it will deter any foreign investor from making house purchases without prior approval.*

- *Ultimately deterrence will be determined by effectiveness of investigatory powers and ability to detect purchases.*

c. **Is the proposal to extend accessorial liability an effective way to increase compliance?**

- *There are already sufficient sanctions for aiding and abetting (Section 11 of Criminal Code). These rules should be enforced. There is no need for further sanction.*

- *Is there any evidence of widespread involvement of Australian accessories in assisting foreign persons in bypassing the FIRB process? As above, funding could be better used to monitor the market and provide data on how to effectively deter the practice if it exists.*

- *The obvious concern for such a regime is that it will encourage foreign investors to provide false information or conceal details from their Australian representatives. This may make it difficult for Australian industry representatives to give good advice to foreign national clients and to encourage them to embrace the FIRB approval process.*

i. **Are there alternative approaches that should be considered?**

- *The use of oral discussions, exchange of letters and other well recognised regulatory structures outside of litigation and the use of the courts, is one that we strongly recommend. The removal of FIRB's ability to engage with investors (which is likely to result from introducing a penalty regime) will have the self-defeating impact of FIRB ceasing to be informed of investment that has occurred.*

d. **Is it necessary to increase the existing criminal penalties in light of the proposed new civil penalties?**

- *A strong criminal deterrent is already part of the regime. However, imposing civil penalties and then higher criminal penalties may have a chilling effect on investment that would otherwise have come to Australia.*

4. **Should the new penalty regime be extended to business, commercial real estate and agricultural applications?**

- *No, it should not. In our experience, the overwhelming majority of foreign investors considering investing in business, commercial real estate and agricultural applications, are very concerned to ensure they comply with the law. That may be due to the larger amounts at stake and/or a greater concern to protect their reputations. We consider that for such investors, greater clarity in the requirements, and better funding to allow FIRB to provide greater guidance, would be far more effective in increasing compliance than a penalty regime. Indeed, we expect that the introduction of a penalty regime would be a handicap and a distraction for FIRB.*

- *We are not aware of any data suggesting unacceptable levels of contravention by foreign investors of the FIRB rules in the areas of business, commercial real estate or agriculture.*

- *It is unclear how breaches in the business sector would be detected given that there is no ready data point to check compliance (the State / Territory Land Titles offices provide data points for real estate applications but there is no equivalent data point for business applications).*

ADVANCED OFF-THE-PLAN CERTIFICATES

5. **The government seeks feedback on the proposed changes to advanced off-the-plan certificates, including:**

- *The aim of advanced-off-the plan certificates is to assist developers to sell units in their developments. This includes to foreign buyers. Imposing penalties will not assist them to do so. The impact of increased fees and penalties will simply result in this beneficial approval not being used and foreign investors will have to make their own applications adding significant extra applications to FIRB's work load.*
- *There is no attraction to a developer to utilise the process given the proposed fees and penalties.*

a. **Should penalties be introduced for developers that fail to comply with obligations to market domestically?**

- *There appears to be a lack of substantiated data that proves developers are failing to comply with obligations to market domestically.*

- *Penalties should not be introduced for developers that fail to comply with obligations to market domestically.*

i. **If so, what should developers be required to do to prove they have marketed domestically?**

- *In accordance with the current regime, developers should be required to provide a copy of their strategic marketing plan to be used in Australia to prove they have marketed domestically.*

ii. **What level of penalty would be appropriate for developers that fail to comply with obligations to market domestically?**

- *Subjecting developers to the risk of harsh civil and criminal penalties is likely to stifle investment in property development. It undermines the ability of developers to source the global capital they need to secure their projects.*

- *The penalties on developers may send a signal to both Australian developers and foreign investors that Australia is not open for investment.*

- *In addition to the proposed penalties, the proposed fees may decrease Australia's comparative advantage if opportunities for foreigners with similar rates of return on investments are available in countries with no fees or such*

penalties. This may then result in the developer not being able to raise appropriate revenue to complete their development.

iii. **Are there alternative approaches that should be considered**

- *The original aim of advanced-off-the-plan certificates was to balance providing developers with a marketing assistance tool and to ensure that domestic buyers have the same opportunity to purchase.*

- *In order to achieve this policy objective, it is recommended that the sale of units to foreign persons be limited to 50%, as was the case for the off the plan policy when it was first introduced.*

- *The requirement for individual approval for acquisitions of off-the-plan apartments valued in excess of $3 million in a single development:*

    - *may not be realistic in some developments*
    - *may be a disincentive for developers to use the process*
    - *is unlikely to assist with the government's screening process of high wealth investors and monitoring of potential criminal behaviour on the part of a potential foreign investor.*

- *While it is sensible for Australian policy to encourage foreign investment in new housing stock, should the policy not go further? Shouldn't the Government be concerned about the scale and location of developments offered to foreign buyers off the plan and whether such developments are satisfying Australian development needs?*

IMPLEMENTATION OF AGRICULTURE COMMITMENTS

6. **Should the definition capture all primary production businesses as well as certain first stage downstream businesses beyond the farm gate (for example, meat processing, sugar milling and grain wholesaling / storage / milling)?**

- *The definition of agribusiness should capture certain first stage downstream businesses beyond the farm gate, as many of these businesses align with the common understanding of what is an agribusiness.*

- *To do so, the definition should incorporate:*

    - *companies / trusts / businesses which own and operate primary production businesses on agricultural land; and*

    - *businesses which are primarily directly engaged with primary production businesses (for example flour mills, sugar mills, grain traders, raw produce carriers).*

The definition should not be extended to cover operations that do not deal primarily directly with the primary producer – eg food and beverage manufacturers.

7. **If it is decided that the ANZSIC codes be used, which divisions (or sub-divisions, groups) of the ANZSIC codes should be included in the definition for 'agribusiness'?**

- *The ANZSIC codes are agreed industry standard definitions developed by the Australian Bureau of Statistics and Statistics New Zealand.*

- *We submit that Division A – Agriculture, forestry, fishing and hunting should be included in the definition for "agribusiness".*

8. **Is there an alternative approach that should be considered to define agribusiness?**

- *Incorporating the definition of primary production business in section 995-1 of the Income Tax Assessment Act 1997?*

- *Section 995-1 provides:*

  You carry on a primary production business if you carry on a primary production business of

  (a) cultivating or propagating plants, fungi or their products or parts(including seeds, spores, bulbs and similar things), in any physical environment; or

  (b) maintaining animals for the purpose of selling them or their bodily produce (including natural increase); or

  (c) manufacturing dairy produce from raw material that you produced; or

  (d) conducting operations relating directly to taking or catching fish, turtles, dugong, beche-de-mer, crustaceans or aquatic molluscs; or

  (e) conducting operations relating directly to taking or culturing pearls or pearl shell; or

  (f) planting or tending trees in a plantation or forest that are intended to be felled; or

  (g) felling trees in a plantation or forest; or

  (h) transporting trees, or parts of trees, that you felled in a plantation or forest to the place:

    (i) where they are first to be milled or processed; or

    (ii) from which they are to be transported to the place where they are first to be milled or processed.

9. **The government seeks feedback on the proposed definition for 'agricultural land':**

- *Comments generally on the definition of "land":*

- *The Foreign Acquisitions and Takeovers Act 1975 ("**FATA**" or the "**Act**") should not incorporate definitions of the different types of land proposed – such as agricultural land, residential land etc. FATA should only make reference to "land".*

- *The regulations should refer to the different subcategories of land - agricultural land, residential land etc along with proposed definitions of each subcategory of land and the approach to each category and relevant exemptions.*

a. **Is the proposed definition of 'agricultural land' consistent with common understanding of the term?**

- *The proposed definition of agricultural land as "land that during the past five years has been used for carrying on a business of primary production. That is:*

  - *land used primarily for the purposes of carrying on, or otherwise supplying, an Australian agribusiness";*

  - *land likely to be used primarily for the purposes of carrying on, or otherwise supplying, an Australian "agribusiness"; or*

  - *land which was, in the five years prior to its purchase, used primarily for the purposes of carrying on, or otherwise supplying, an Australian "agribusiness",*

  should not be adopted.

- *The proposed definitions:*

  - *do not adequately address the character of the land at the time of the acquisition;*

  - *do not consider that land may have changed use (eg. from rural land to developed commercial property) – particularly for land which was, in the five years prior to its purchase, used primarily for the purposes of carrying on, or otherwise supplying, an Australian "agribusiness";*

  - *are too broad in scope – particularly for land which is "likely to be used primarily for the purpose of carrying on, or otherwise supplying, an* Australian "agribusiness".

i. **Are there alternative approaches that should be considered?**

- *It is recommended that:*

  - *the current definition of rural land be adopted but amended to be – "land used for the <u>dominant</u> purpose of carrying on of a primary production business at the time of the acquisition".*

- *alternatively, the first suggestion could be - "land used primarily for the purposes of carrying on, or otherwise supplying, an Australian agribusiness, at the time of the acquisition".*

b. **Would the proposed definition provide sufficient clarity as to what constitutes 'agricultural land' for the purposes of Australia's foreign investment framework?**

- *the proposed definition stated in 5)a)i):*
  - *provides sufficient clarity as to the dominant use of the land by introducing a "dominant purpose" test (so as to capture land that may be used for multiple purposes such as a bed & breakfast on a farm or a restaurant at a winery); and*
  - *adequately characterises the nature of the land by including "at the time of the acquisition" in a way that sufficiently limits the scope of the definition while also enabling the government to screen purchases that reflect a common understanding of what agricultural land is.*

10. **The government seeks feedback on the proposed definition of urban or 'residential land', including:**

a. **Is the proposed definition of 'residential land' consistent with a common understanding of the term?**

- *"land (that is not agricultural land) used, or to be used, for the purposes of one or more residential dwellings"*
- *The definition is workable but should be amended to exclude other types of land as set out below. The definition does not assist with mixed use properties (eg residential above a shop, or a janitor's apartment in a commercial building). A definition must be clear as to dominant purpose to avoid the concern raised regarding rural land with mixed uses. Further, as noted above, separate definitions should not be used in the Act but rather as a category of land addressed by the Regulations*
- *The committee also refers to paragraph 13 of the WHT Review, which similarly grapples with difficulty of the description of "residential property", particularly looking at how it is defined in relation to acts relating to first home buyers, taxation, or GST. The Committee believe that a more detailed discussion needs to take place in terms of agreeing on a suitable definition, noting that a different definition in each of acquisition, transactional, taxation, and social legislation creates uncertainty, ambiguity and inefficiency.*

i. **Are there alternative approaches that should be considered?**

- *"land (that is not agricultural land, developed commercial property … [insert other categories of land]) used, or to be used, for the dominant purpose of one or more residential dwellings"*

b. **Would the proposed definition provide sufficient clarity as to what constitutes 'residential land' and related subcategories (such as new and existing dwellings) for the purposes of Australia's foreign investment framework?**

- *If amended as suggested the definition would assist with clarity.*

11. **The government seeks feedback on three possible options for the screening of 'other land':**

a. **'Other land' be defined as all land that is not 'agricultural land' or 'residential land' and continues to be screened from dollar zero;**

- *This is undesirable. See comments below.*

b. **'Other land' is not defined and any land that is not 'agricultural land' or 'residential land' no longer requires foreign investment approval; or**

- *This is undesirable. See comments below.*

c. **'Other land' is defined as a subset of what is left over from 'agricultural land' or 'residential land' capturing land that remains of interest while excluding some land from screening.**

- *This is undesirable. See comments below.*

i. **If option c is pursued, what types of land should continue to be screened?**

- *It is undesirable to have a definition of "other land". The objective of this catch-all definition is unclear. It does not address the policy concerns of foreign persons acquiring interests in rural / agricultural land, residential land etc.*

- *Instead, it is proposed that the regulations list and define the different categories of land. These may include:*

- *rural / agricultural land;*

- *residential land;*

- *vacant land;*

- *developed commercial property;*

- *mining tenements;*

- *the seabed etc.*

12. **The Government seeks feedback on implementation issues around the foreign ownership of land register, including:**

- *It is unclear to the Committee of the purpose and effect of the proposed register and its interaction with the existing Land Titles Office registers. Is "registration" on the foreign ownership register, simply intended to act as a record, or is the act of registration intended to create some legal right or create some evidential onus? How does listing on the Register effect Torrens Title rights? Is the register to be searchable? The Committee suggests further thought and discussion needs to take place as to the interaction of the proposed register and the existing Land Titles Office registries.*

a. **the foreign ownership details that would be collected and published by the register;**

- *The register should collect information on the legal title holder of the property, their country of control (noting the tracing provisions of the FATA), the address of the property and the consideration paid for the property.*

- *If the register is to be made public it is undesirable for the country of control of the purchaser to be made public for privacy reasons. Statistics on the country of control of purchasers could be published at the end of each financial year.*

- *It is not clear if the register will use the same definition of "foreign" as in the foreign investment regime. If so, will the register also use a tracing mechanism (as suggested above)?*

- *It is not clear if the register will track acquisitions of companies / trusts that own rural land (or are rural land rich) as well as direct interests in rural land.*

b. **the two-stage implementation approach to information collection (through self-reporting then through state and territory land titles processes); and**

- *As a suggestion, State and Territory land titles offices could collect information on purchasers at the time stamp duty is collected / the land title document is registered with the new purchaser.*

- *The Committee, with input from the Australian Property Law Group of the Legal Practice Section of the Law Council, is opposed to the implementation of a requirement for State and Territory land title processes to be altered in order to record on the Land Titles Office register the country of origin/control of a purchaser. A Torrens Register is a system of title by registration not registration of title. The Register creates and records interests in land – it is not a collection tool for various other arms of Government. To impose "country of origin/control" as a compulsory field in the LTO registries requires legislative change across each of the State and Territory jurisdictions. Changes are needed to Torrens, Real Property or Land Title legislation, the National e-conveyancing laws, and (if Revenues Offices are included) to Duties legislation. It also requires industry wide changes to the property and banking sectors. Standard mortgage documents will need to be*

changed, standard Contracts for Sale developed by Law Societies or Institutes will need to be changed and an extensive education process embarked upon. These changes will create a significant cost for the property sector, and will increase the time taken, and cost associated with simple transactions. As an exercise in legislative reform it would be a significant change to the existing property law framework within the country.

- *Putting the obligation upon lawyers to satisfy themselves as to the country of origin / control of their client, takes the role of the lawyer beyond its current one, in essence making them a "de-facto guarantor" of the client that they are representing. The effect is that practitioners then take some personal accountability for obligations of their client. This imposes a significant and unfair obligation on the practitioners, which does not currently exist.*

c. **how lawyers or register conveyancers would verify whether their client is a foreign person?**

- *The suggestion of using lawyers/conveyancers to be responsible for registration fails to understand the nature of the lawyer / client relationship. The lawyer is acting for the client for these purposes and ought not to be in a position of effectively acting for the government. Further, the proposal does not cover all avenues as many transactions are conducted by the foreign entity themselves without lawyers and conveyancers*

- *Using FATA's existing foreign person definition, as is the case currently. Lawyers and conveyancers should already be aware of the obligations under the FATA and Policy and can advise clients regarding their "foreign" status but ought not to be made responsible for their clients actions.*

- *Some of the issues associated with the identification of whether a client is a "foreign person" have been dealt with in length in the WHT paper with which this Committee concurs. Some of the complexities relating to corporate entities are canvased at length in that paper and should be considered.*

MODERNISING AND SIMPLIFYING THE FOREIGN INVESTMENT FRAMEWORK

13. **The Government seeks feedback from interested stakeholders on options to modernise and simplify the Act, Regulations and Policy and streamline interaction between applicants and the Foreign Investment Review Board.**

Attached is the submission made by the Business Law Section of the Law Council in 2014 regarding suggested amendments to Australia's foreign investment regime. We emphasise, however, that any amendments should not be rushed, especially if the changes are extensive or complex.

- ***Speeding up the review process:***

- *The current 30 day and 90 day review processes (plus 10 day notice periods) and gazetting of interim orders leads to the current practice of withdrawing and resubmitting applications when the 30 day time period cannot be achieved. This has resulted in unnecessary red tape and cost and leads to perceptions of a lack of transparency as a process outside the statutory framework.*

- *In practice, no time frames surround decisions made under the Policy. The lack of time frames is not conducive to discipline around responsiveness on such applications, particularly where they relate to relatively routine matters.*

- *We suggest that the legislation be amended to reflect the following regime:*

    - *Decisions under the legislation and Policy to be made within 30 days of an application being made.*

    - *The review period can be extended by up to 90 days by the Treasurer or such other period agreed by the applicant.*

    - *Extension of the review period is not an interim order that requires publication in the Gazette.*

    - *The "one size fits al"l approach of the current framework is frustrating for foreign investors, especially those whose cases comprise the overwhelming majority of business notifications that are cleared. Procedures and potentially safe harbours should be developed so that these cases are cleared in substantially less than 30 days or don't require clearance at all.*

    - *Consideration should be given to an exemption power for particular cases or classes of cases. An example would be an acquisition by a fund in which a foreign limited partner investor (with no control at all) has a small and/or passive holding.*

- ***Streamlining FATA and Policy***

- *The FATA legislation and the foreign investment regulatory regime more generally is overly complex and impenetrable to foreign investors. The regime is unnecessarily complicated by the separate Policy and confusingly the FATA makes no reference to FIRB, its composition or its role.*

- *The complexity contributes to the concerns with transparency of the process. A simpler and more accessible presentation of the legislation and regulatory requirements would assist in promoting Australia as an investment destination to investors especially as many foreign investors may have English as a second language.*

- *The Policy contains substantive regulation that is not contemplated by FATA (e.g. in relation to media or SOEs).*

- *Legal representatives consistently receive questions from clients asking to outline whether their particular applications fall under the FATA or under Policy.*

- *Changes to the Policy are not subject to public consultation or in some cases notification. Material changes to the Policy should at the least be subject to public consultation. This is particularly concerning given that many applications fall under Policy. It would be useful where the Policy is updated to make available a comparison document to highlight changes from the prior Policy.*

- *Substantive regulations should be legislated under FATA with the Policy restricted to guidance as to how the substantive regulation is reviewed and implemented.*

14. **Are there harmonisation opportunities with other Acts (e.g. the operation of the *Insurance Acquisitions and Takeovers Act 1991* or the *Financial Sector (Shareholdings) Act 1998*? Should the definition of 'Associate' in the Act conform with the definition of 'Associate' in the *Corporations Act 2001*?)**

    - *The FATA should be updated to reflect modern business practice, and regulatory concepts and terminology in a similar way to that used in other legislation.*

    - *The FATA has not been modernised for modern corporate finance concepts and practices. The attached Business Law Section submission makes a number of recommendations in this regard.*

    - *Any requirement for approval should apply equally to the form of the investment e.g. direct, trust, company, partnership, limited partnership etc.*

    - *The definition of "associate" found in s6 of the FATA is unworkably broad. The FATA should use an associate definition based on the Broadcasting Services Act 1992 (or similar) (schedule 3 of the attached Business Law Section submission) which is better suited for the purposes of the foreign investment regime. The Corporations Act contains multiple associate definitions which, in many cases, are more appropriate in the context of public transactions. In any event, we think that it should be clear that a foreign person is not an associate of another investor in the same structure (eg company, trust, limited partnership, unincorporated joint venture etc) merely because they are parties to the governing document or investment agreement (eg shareholders agreement, securityholders agreement, investors agreement or JV agreement) relating to its governance (eg an Australian company should not considered to be a foreign person simply because it has a single 10% foreign shareholder which is party to a shareholders agreement to give effect to the shareholders collective views regarding board composition, voting majorities, pre-emptive rights, gearing, dividend policy etc).*

    - *To conform to international standards and reduce red tape, the requirement for any FIRB approval under FATA should be a condition precedent to completion of the transaction and not to the entry into (or formation) of the agreement (see section 26(2)). Some global transactions which are subject to a condition that all required foreign investment and anti-trust approvals are obtained prior to completion do not technically comply with FATA as it adopts an unusual formulation for the required condition.*

- *There is no need for a double up of applications under the Financial Sector (Shareholdings) Act 1998 and the foreign investment regime (both FATA and Policy), particularly as applications under both regimes are considered by the Treasurer. This double up adds cost, time and additional red tape to proposals.*

- *The definition of "foreign government investor" is too broad, and inadvertently captures many investors who would not ordinarily be considered a foreign government investor. Either narrowing the definition, or increasing the existing thresholds from 15/40 to 20/50 could remove some unnecessary administrative applications from the foreign investment regime.*

15. **Is the current regime for enforcement of FIRB conditions effective? What alternative measures could be considered?**

    - *Dedicated officer(s) at the Foreign Investment and Trade Policy Division should be allocated to follow up on compliance with conditions in residential real estate, commercial real estate, agriculture and business approvals.*

16. **Should FIRB provide specific regulatory guidance on approaches to applications and difficult interpretation issues like Australian Securities and Investments Commission and the Takeovers Panel do?**

    - *Guidance from FIRB is to be encouraged, where appropriate.*

    - *Given the proposal for fees to be paid and the potential for increased penalties, the guidance provided should be very substantially improved from that currently available.*

    - *Provision of guidance on applications and interpretation issues will provide greater transparency and predictability to the FIRB process. It may make the FIRB process appear less secretive and hostile to foreign investors, for which the Australian screening process is often criticised internationally.*

Attachment - Further Comments on Penalty Regime

Introduction

Set out below are more specific comments in relation to the particular questions raised in the Options Paper. We set out here some preliminary comments on the best options that we believe should be considered by Government in evaluating whether the current penalty regime operating in relation to Australia's foreign investment framework might be amended.

The question of the level of penalties for breaches of commercial legislation ranging from corporate law to competition law (and all matters in between) has been the subject of very lively, and at times quite extraordinarily uninformed, debate in the media and elsewhere. A central theme that we believe should be observed in any penalty regime that the Federal government is responsible for is that the regime should be carefully structured, should be simple, and should reflect the concerns that have been established in the community as being relevant in the context of breaches of the particular regime under consideration. The regime should be carefully structured, and in all cases should be able to be justified on the basis of reliable evidence relating to the failure of the current regime.

There is unreliable evidence, in our view, to suggest that anything other than a simple, and carefully designed penalty regime, one that recognises the options that are available to the regulator in dealing with alleged non-compliance, should be imposed.

In our view the infringement notice regime, suggested in the options paper, is neither relevant nor suitable to the regulation of Australia's foreign investment framework. We make these comments by reference to the significant amount of work that the Law Council's Business Law Section has undertaken in dealing with the initial proposals to introduce the infringement penalty regime into Australian law. The Australian Law Reform Commission in 2003 strongly recommended against the introduction of the infringement notice regime into corporate law. Despite strong representations made by a wide section of the business and legal communities, the government chose to introduce the regime into the corporate law area to deal with alleged breaches of the continuous disclosure regime operating in the Corporations Act. It was suggested by the Federal Treasurer, the Honourable Peter Costello at that time, that this legislation would operate as a temporary measure to be reviewed.

Whilst a review may have taken place in 2007, the results of such a review were never made public. Ongoing work undertaken by the Business Law Section, together with organisations such as the Business Council of Australia and the Australian Institute of Company Directors in 2012, (details of which have been provided to the previous Labor Government and to the

representatives of the then opposition, -now the current government) in 2013, illustrate that the infringement notice regime should be the subject of careful review. It was also our view that the regime should not be extended as a matter of course to other areas of business law.

Despite these representations, the infringement notice regime has now been extended to apply to a number of other areas of the law and regulation. To simply add this regime, as suggested in the options paper, to the regulation of foreign investment, would be a regrettable decision in light of the concerns raised by the Business Law Section and other bodies. Before a major civil penalty regime is introduced, careful consideration should be given to the alternatives to the imposition of penalties in situations where alleged breaches of the law may be said to have occurred. These are well understood in the regulatory environment, and there is plenty of experience of the use of alternative measures and procedures that can be usefully used as precedents in structuring an appropriate regime for the current foreign investment framework.

The use of oral discussions, exchange of letters and other well recognised regulatory structures outside of litigation and the use of the courts, is one that we strongly recommend that should be considered as relevant for modification and the use in the context of any penalty regime that may be included in the current proposals.

Law Council
OF AUSTRALIA

Business Law Section

Executive Member
Foreign Investment Review Board
The Treasury
Langton Crescent
PARKES ACT 2600
Via email:

19 June 2014

Attention: Jonathan Rollings

Dear Sir or Madam,

Submission for a reform of Australia's foreign investment regime

We refer to the meeting between representatives of the Business Law Section of the Law Council of Australia (BLS) and your colleagues Jonathan Rollings, Paul Flanagan, Andrew Deitz and David Earl from the Foreign Investment Review Board at Treasury in Canberra on 1 May 2014 to discuss possible reform of Australia's foreign investment regime.

As discussed at that meeting, please find enclosed a submission from the BLS on possible amendments to Australia's foreign investment regime. The submission identifies a number of:

- "quick fixes" at section 1 and Schedule 1 which could be quickly and non-controversially introduced; and
- more substantive issues and broader root and branch review for further discussions.

We would be pleased to meet with you to discuss any aspect of our submission. If you have any queries concerning the submission please contact Malcolm Brennan or myself as follows:

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Yours faithfully,

John Keeves
Chairman, Business Law Section

Enc.

Amendments to Australia's Foreign Investment Regime

The Business Law Section of the Law Council of Australia (**BLS**) supports amendments to the *Foreign Acquisitions and Takeovers Act 1975* (Cth) (**FATA**), the associated regulations (**FATR**) and the Australian Government's Foreign Investment Policy (**Policy**). The BLS submits that it is timely to consider making non-controversial amendments in 2014 at the same time as any amendments concerning rural land.

Foreign investment is critical to Australia. Australia's success has been built on its access to foreign direct investment from a variety of capital rich countries over time. An ongoing welcoming attitude to foreign direct investment is critical for the development of Australian infrastructure and competiveness over the next decades.

There have been concerns raised over the last few years about the transparency and clarity of Australia's foreign investment rules. Thresholds for foreign investment approvals have also been a key feature of the recent free trade agreements (**FTAs**) negotiated by Australia (and of the Australia/China FTA currently under discussion).

There is much that can be done to improve the perceived transparency of the process by updating it for current practices (many of which have moved on considerably since 1975), simplifying the language of the legislation and policy, removing inconsistencies and red tape and reducing processes which are currently conducted outside the legislation itself.

The BLS makes the following suggestions to achieve the objectives of effective regulation, minimising red tape and increasing transparency. Over the longer term, we would strongly support a broader root and branch modernisation of the foreign investment regulatory regime. We would be pleased to meet with you to discuss with you any aspect of our submissions below.

1 Some quick fixes could be easily introduced

BLS members have identified a number of areas where fixes to the regime could be quickly and non-controversially introduced. Those "quick fix" changes are identified in Schedule 1.

The BLS submits that these areas cause unnecessary cost and inefficiency to the operation of the regime that could be relatively easily corrected.

BLS Recommendations:

- include red tape amendments in the next amending bill; and
- allow for public consultation on red tape amendments.

2 Regulate investments by sovereign wealth funds (SWF) and state owned enterprises (SOE) more effectively to meet policy objectives

The BLS considers that the manner in which SWF and SOE investment is regulated is a pressing area for reform given how important investment by these types of investors has become.[1]

The BLS understands public concern that the Australian Government should be aware of what foreign governments are doing in Australia and government policy concerns that there is a risk SWF and SOE investments might not be commercial in nature or could be undertaken in pursuit of political or strategic objectives that may be contrary to Australia's national interest.

[1] As at the end of 2013 it has been estimated that SWFs held assets of at least US$6.2 trillion. Some of the largest commercial enterprises in the world are SOEs.

However, the BLS is concerned that the current regulation of SWF and SOE investments is not targeted to address these policy concerns. In addition, despite the large investment by SWFs and SOEs in Australia over recent years there is no evidence that these concerns are justified in respect of most SWFs and SOEs.

Under the Policy all foreign government investors must notify and get prior approval before making a direct investment in Australia, regardless of the value of the investment. However, a foreign government investor is defined broadly and simplistically to include entities in which governments, their agencies or related entities have an interest above a prescribed threshold (15% from a single country or 40% from more than one country).

Such a definition ignores significant differences in the types of entities that have a degree of government ownership.

The A$0 threshold for direct investment by foreign government investors is also extremely low by international standards.[2] As such, even routine or immaterial activities are technically subject to formal review.[3]

The fact that other countries do not have such controls or have higher review thresholds suggests that the current approach imposes unnecessary costs for SWFs and SOEs undertaking foreign direct investment in Australia.

There is a significant difference between an investment by a foreign government or its instrumentalities and most investments by SWFs or SOEs. That difference should be recognised in Australia's regulatory regime.

Sovereign Wealth Funds (SWFs)

SWFs are a heterogeneous group and the influence of government is always present, as it is in SOEs. Nevertheless, SWFs may be more readily distinguishable from SOEs as special purpose funds or arrangements owned by the general government.[4] They are commonly established from balance of payments surpluses, official foreign currency operations, the processes of privatisations, fiscal surpluses and/or receipts from commodity exports.

The influence of government ownership upon SWFs and their investment strategies may be less direct than it is for SOEs and more predictable. SWFs hold, manage or administer assets to achieve financial objectives and they employ a set of investment strategies that include investing in foreign financial assets.[5] For these reasons, the International Working Group of SWFs has been able to establish 24 generally accepted principles and practice (**GAPP**) for SWFs (**the Santiago Principles**).[6]

More generally, SWFs have been perceived as valuable sources of long term institutional capital and as an important force for market stabilisation. For these reasons, a more express welcoming attitude to SWF foreign direct investment would benefit Australia's national interests having regard to the ongoing importance of SWFs in areas such as the development and operation of infrastructure.

Over the last decade significant supranational work has been undertaken to advance transparency and independence of SWFs through the development of the Santiago principles. Australia was at the forefront of those efforts. Australia's regulatory regime should recognise and encourage adherence to the Santiago principles.

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[2] For example, in Canada, SOE investments are subject to a monetary threshold of a book value of assets of C$354 million in 2014.
[3] A good example would be the purchase of an Australian incorporated shelf company.
[4] *Sovereign Wealth Funds: Generally Accepted Principles and Practices* (**the Santiago Principles**), International Working Group of Sovereign Wealth Funds, 2008 at 3.
[5] See note 4.
[6] See note 4.

State Owned Enterprises (SOEs)

An SOE is a commercial enterprise where the state has significant control through full, majority or significant minority ownership.[7] We are not aware of any evidence of SOEs pursuing investment activities for political purposes.

BLS members advising SWFs and SOEs have first-hand experience as to the significant cost and red tape compliance issues experienced by SWFs and SOEs in complying with the Australian regime. Further, BLS members have first hand experience with the delays and red tape issues experienced by Australian business in interacting with SOE's and SWF's in commercial dealings.

The BLS makes the following draft recommendations for change to the general regime. In addition, BLS members have experience of a further subset of technical issues that should be unobjectionable from a policy perspective. Those technical issues are dealt with in Schedule 2 to this submission.

BLS Draft Recommendations:

- distinguish foreign direct investment by governments and their instrumentalities from that of SWFs and SOEs;
- continue to apply existing policy to foreign direct investment by governments and their instrumentalities;
- establish a separate category for SWFs that adhere to the Santiago principles (**recognised SWF investors**);
- provide a mechanism for an SWF to be certified as a recognised SWF investor following an initial screening by FIRB of its governance structure and investment mandate. That certification may be general or for certain categories of investment that accord with the investment mandate of the SWF investor;
- apply the general review threshold to a recognised SWF investor;
- provide that a recognised SWF investor must provide annual reports to FIRB of their foreign direct investment activities in Australia and notify any changes relevant to its certification as a recognised SWF investor;
- establish a separate category for certain SOEs (**recognised SOE investors**);
- provide a mechanism for an SOE to be certified as a recognised SOE investor following an initial screening by FIRB of its governance structure and commercial objectives;
- apply an increased approval threshold to a recognised SOE investor to facilitate immaterial or ordinary course investment activities in Australia (say $50 million); and
- provide that a recognised SOE investor must provide annual reports to FIRB of its foreign direct investment activities in Australia and notify any changes relevant to its certification as a recognised SOE investor.

[7] Definition taken from *OECD Guidelines on the Corporate Governance of State Owned Enterprises.*

3 Streamline submission and review process to reduce red tape

The BLS is concerned that the current 30 day and 90 day review processes (plus 10 day notice periods) and gazetting of interim orders leads to the current practice of withdrawing and resubmitting applications when the 30 day time period cannot be achieved. This has resulted in unnecessary red tape and cost and leads to perceptions of a lack of transparency as a process outside the statutory framework.

The BLS is also concerned that in practice, no time frames surround decisions made under the Policy. The lack of time frames is not conducive to discipline around responsiveness on such applications, particularly where they relate to relatively routine matters.

According to ITS Global, the delay on all inwards foreign investment subjected to review represents a permanent and ongoing cost to the domestic economy, being the return foregone on the investment approved by the Government over the period of the delay. Based on 2006-07 data, ITS Global estimate the economic cost of the delayed investment is around $4 billion a year.[8]

BLS Recommendations:

- remove or shorten the 10 days' notice periods for decisions made;
- remove the requirement to gazette interim orders if the applicant agrees to a confidential extension;
- provide the Treasurer the ability to issue an extension of up to 30 days in the rare instances more time is required; and
- apply the same statutory timeframe to reviews under the Policy.

4 Simplify the general thresholds for review

The BLS is concerned that there are too many thresholds for review, which levels are not proportionate to the level of sensitivity associated with the investments.

The current threshold for review of A$248 million for general investments (A$1,078 million for US, New Zealand (**NZ**) and (shortly) Korea and Japan) is low by international standards.[9] As noted before, the A$0 threshold for direct investment by SOEs is extremely low by international standards. The myriad of thresholds for real estate could also benefit from a review. By way of example, the threshold for interests in Australian urban land (which can cover mining projects) is effectively zero.

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[8] '*Foreign Direct Investment in Australia — The Increasing Cost of Regulation*' (Report, ITS Global, 2008), 21. This estimate is based on inwards approved investment of $156.4 billion in 2006-07 and an assumed weighted average delay of three months for each approval, weighted by the value of the proposed investment. The Social Opportunity Cost of the capital foregone by the delay is assumed to be 10 per cent a year. The cost of withdrawal is estimated to be at approximately $1.5 billion a year.

[9] For example, in Canada, the general threshold for a World Trade Organization (**WTO**) member is C$354 million in 2014. Under the amendments to the Investment Canada Act as proposed in the Economic Action Plan 2013 Act (which will commence upon an order of the Governor in Council), this threshold is to be increased substantially to an enterprise value of C$600 million, rising to C$1 billion over four years. The general threshold in Canada for a non-WTO member is C$5 million for direct investments and C$50 million for indirect transactions.

The BLS considers that the appropriateness of the thresholds should be assessed against a risks and benefits framework based on policy concerns, so that only high risk investments are subject to review, but not otherwise. The great majority of transactions submitted for review are approved,[10] suggesting that most of the transactions may be low risk.

BLS Recommendations:

- simplify the general review thresholds so there are fewer thresholds proportionate to the level of risks associated with the transactions;
- tie the general review thresholds to 50% of the thresholds under the FTAs; and
- ensure the proposed agriculture investment review thresholds are not disproportionate in light of the general review thresholds.

5 Move to a broader root and branch modernisation of the foreign investment regulatory regime

The BLS is concerned with the complexity of the FATA legislation and the foreign investment regulatory regime more generally. The regime is further complicated by the separate Policy. The complexity contributes to the concerns with transparency of the process. A simpler and more accessible presentation of the legislation and regulatory requirements would assist in promoting Australia as an investment destination to investors especially as many foreign investors may have English as a second language.

For example:

- the FATA has not been modernised for modern corporate finance concepts and practices. Any requirement for approval should apply equally to the form of the investment e.g. direct, trust, company, partnership, limited partnership etc;
- the Policy contains substantive regulation that is not contemplated by FATA (e.g. in relation to media or SOEs);
- changes to the Policy are not subject to public consultation;
- the FATA makes no reference to FIRB, its composition or its role;
- an expansion of the sanctions available for enforcement of the legislation; and
- review of the appropriateness of the "aggregate substantial interest" concept whereby a foreign person acquiring even a single share in a company which has greater than 40% foreign ownership may be potentially subject to divestiture if the acquisition is contrary to the national interest (even if the acquired stake is small enough as to not require prior notification and approval).

[10] In 2012-13, a total of 13,322 applications for foreign investment approval were considered, with 12,731 approved, none rejected, 446 withdrawn and 145 exempt as not subject to the Policy or the Act: Foreign Investment Review Board Annual Report 2012-13 (2014), 9.

BLS Recommendations:

- update the FATA to reflect modern business practice, and regulatory concepts and terminology used in the Corporations Act;
- incorporate substantive regulation into the FATA with the Policy restricted to guidance as to how the substantive regulation is reviewed and implemented;
- subject material changes to the Policy to public consultation;
- recognise the FIRB's composition and role formally in legislation to improve transparency and accountability;
- review sanctions and administration of FATA; and
- consider operation of definitions of "aggregate substantial interest" and "aggregate controlling interest".

SCHEDULE 1
QUICK FIX CHANGES

1. Obviously outdated and otiose exemptions – moneylending agreement

There are a number of obviously outdated and otiose exemptions in the FATA and FATR. For example, the exemption for moneylending agreements (FATA s5) needs to be updated to deal with the proliferation of different kinds of lender/arrangements.

BLS Recommendations:

- amend definition for moneylending agreement in FATA to conform to section 609(1) of the Corporations Act as modified by ASIC class order 13/520.

2. Obviously outdated and otiose exemptions – real estate sector

Also, relevant to the real estate sector, there are a number of outdated and ineffectual exemptions:

- the exemption at FATR 3(o) refers to an acquisition of units in a unit trust that accepts funds from the public on the basis of a prospectus approved by the Corporate Affairs Commission of a State or Territory which no longer applies; and

- the exemption at FATR 3(p) refers to an acquisition of land which is entered in the Register of the National Estate which no longer exists.

As an interim measure to provide some relief to the real estate sector, before the regulation is formally put through Parliament, FIRB has announced that no action will be taken when a foreign person does not notify and seek prior approval in relation to an acquisition of a passive interest in a listed or unlisted Australian urban land trust estate, by acquiring an interest in units that result in a holding (alone or with associates) of less than:

- 10% in a listed trust, with a predominantly non-residential property portfolio of office, retail, industrial, or specialised properties, or a mix of these; or

- 5% in other public trusts with at least 100 unit holders and whose developed residential real estate assets that have been acquired from non-associates are less than 10% of the target trust's real estate assets.

In legislating the interim measures as amendments to the FATR, we suggest each interim exemption be lifted to 15% to be consistent with the "substantial interest" threshold throughout the regime.

BLS Recommendations:

- amend FATR 3(o) to exempt acquisition of interest of less than 15% in managed investment schemes regulated by Chapter 5C of the Corporations Act (or alternatively listed or other widely held managed investment schemes);

- amend FATR 3(p)(B) to clarify that the reference to "Register of National Estate" is to all heritage listings; and

- amend FATR 3(p)(ii) to clarify that the valuation threshold applies to the "interest in Australian urban land" rather than the "land" as it is more appropriate to refer to the value of the interest rather than the entire property where a person is seeking to acquire less than a 100% interest in a property. Or create an exception for less than 15% interests in land that meets the threshold.

3. Add exemptions for uncontroversial transactions to remove red tape

There are a number of uncontroversial transactions currently subject to approval, where there are no discernible policy concerns. If FIRB has concerns as to some aspects of the transactions listed the obligation could be changed to an undertaking to report the transaction to FIRB rather than a requirement for approval. For example, review is required for:

- acquisitions pursuant to pro rata offers of shares in companies (under Policy) and units in trusts (FATA and Policy), such as through rights issues or dividend/distribution reinvestment plans;

- acquisitions of shares in listed companies and listed trusts by underwriters who are investment banks provided those securities are sold down to third party investors within a short period (say 30 days) and no voting rights are exercised by the underwriters;

- intragroup transfers where the ultimate controller or the net foreign investment does not change (i.e. there is no "new" foreign person other than an interposed subsidiary of the foreign controller) or where the transaction is tax neutral as it involves a tax consolidated group; and

- acquisitions of additional shares by a foreign person who already holds a substantial interest in a company, even if the acquisition does not result in an increase in the foreign person's shareholding percentage (see FATA ss26(6)(b)(ii) and (iii)).

BLS Recommendations:

- amend the Policy to exempt all acquisitions pursuant to a pro rata offer of interests in shares in companies and units in trusts. For this purpose, an offer will still be considered to be pro-rata if there is a separation between the institutional and retail offer and the offer is not made in certain jurisdictions due to illegality or cost;

- amend the Policy to exempt all acquisitions by underwriters who are investment banks provided these securities are sold down to third party investors within 30 days and no voting rights are exercised by the underwriters;

- exempt all intragroup transfers from FATA ss18 and 26 where the ultimate controller or the net foreign investment does not change. This exemption could be limited to transfers between an entity and a wholly-owned entity or between wholly-owned entities within a corporate group or transfers within a tax consolidated group; and

- limit FATA ss26(6)(b)(ii) and (iii) to circumstances where a foreign person acquires additional shares (or securities convertible into shares) in a company which results in an increase in the person's shareholding percentage (or shareholding percentage assuming conversion of securities convertible into shares).

4. *The troublesome "Associate" reference*

The term "associate" as defined in FATA is anomalous and should be replaced with a more customary definition.

The concept is inherently ambiguous, not linked to action in concert that is normally the hallmark of association and does not sit well with determining association within and across corporate groups. In particular, there are three principal concerns with the definition.

First the infinite repetition under paragraph (l) of the associate test means that people can be associates of each other without even having vaguest idea that this may be the case.

Second the automatic deeming of relationships as giving rise to an association is out of date and ill conceived. By way of example:

- why is a person's employer or employee considered to be an associate (eg a company such as BHP Billiton would have over 100,000 employees to make inquiries of even before considering any other limbs of the associate test).

- the notion of partners being associated would mean that limited partners would be associated for all purposes merely because of their common investment in a small unrelated venture. This would have significant impacts for financial sponsors and their investors.

- even vigorous competitors having a substantial interest in a single joint venture company would be deemed to be associates for all purposes and not just the joint venture. This would have significant implications for the energy and resources sector where joint ventures are a common funding and operating structure and also a means for them to obtain portfolio exposure. It would also have implications for consortium bids which are becoming far more prevalent).

Lastly, unlike the Corporations Act acting in concert test, there is no requirement for any of these deemed relationships to have any connection with the underlying investment.

A well known aphorism used by advisors who deal in this area is that taken to its logical conclusion all members of the human race are associates of each other (section 6(l) definition).[11] At a practical level it makes the prudent task of seeking to identify one's associates impossible in practice.

BLS Recommendation:

- replace FATA s6 with the definition of "associate" taken from the Broadcasting Services Act with appropriate changes (see Schedule 3).

5. *Allow use of more recent auditor-reviewed financial accounts*

Various provisions in the FATA provide that the value of a company's assets is the value shown in the company's most recently audited balance sheet (FATA ss13(4), 13B(1)(a)(i),

[11] Another example is the technical concern that all SOEs of a particular country are associates of each other.

13B(5)(a) and 13C(2)). Such a balance sheet can be up to 12 to 16 months old. Where a more recent auditor-reviewed (as opposed to audited) balance sheet is available, it would be more appropriate to use the more recent balance sheet.

BLS Recommendations:

- extend FATA ss13(4), 13B(1)(a)(i), 13B(5)(a) and 13C(2) to allow the use of an auditor-reviewed balance sheet for a half-year period where it is more recent than the audited balance sheet; and

- amend definition of "last accounting date" in FATA s13(3) to refer to the date of the latest audited financial accounts or auditor-reviewed financial accounts, whichever is more recent.

6. Allow independent valuation of land

In determining whether a company is an Australian urban land corporation, FATA s13C(2) provides that if a reasonable value of a company's land assets is not shown in its last audited balance sheet, the reasonable value shown in the company's accounting records is used. It is unclear how this reasonable value is determined.

In contrast, in determining whether a trust estate is an Australian urban land trust estate, FATA s13D(2) provides for the use of a valuation by a suitably qualified valuer not more than 12 months before the particular time.

BLS Recommendations:

- replace FATA s13C(2)(b) with a valuation by a suitably qualified valuer acting at arm's length in relation to the valuation, not more than 12 months before the particular time, where the value of the assets had not increased significantly between the time of the valuation and the particular time.

7. Remove potential double counting of subsidiary assets

FATA ss13(2) and 13C(3) both provide that, for the purposes of determining asset values under those sections, assets comprising shares in a subsidiary are excluded. This is to avoid a double counting of asset values in circumstances where the assets of a corporation and its subsidiaries are aggregated.

In contrast, FATA s13B does not include an equivalent exclusion with the result that it technically appears to require a double counting of assets – namely the value of the assets of a subsidiary and the value of the shares in that subsidiary (which would already reflect the value of the subsidiary's assets).

BLS Recommendations:

- insert into FATA s13B a paragraph similar to FATA ss13(2) and 13C(3) to exclude assets comprising shares in a subsidiary from the calculation.

8. Remove distinction between substantial interest and controlling interest

Given that, as a result of FATA s9(2), a "substantial interest" or "aggregate substantial interest" in a corporation would only not be a "controlling interest" or "aggregate controlling interest" upon an application being made to the Treasurer for a determination, there seems to be little need to distinguish the two concepts.

BLS Recommendations:

- replace references throughout the FATA to "controlling interest" and "aggregate controlling interest" with references to "substantial interest" and "aggregate substantial interest".

9. Consistent use of references to interest in shares or units

The "substantial interest" concept at FATA ss9 and 9A is defined with respect to "interest in issued shares" (further defined at FATA s11) and "interest in trust estate" (further defined at FATA s12B).

However, other terminology is used elsewhere in the FATA and FATR. For example:

- "interest in a unit" at FATA s12A(f), currently not defined in the FATA;
- "acquisition is of shares" at FATR 3(i) and 3(j); and
- "acquisition is of units" at FATR 3(o).

For clarity of drafting, we consider it desirable that "interest in shares" or "interest in units" be used consistently throughout to line up with the FATA's definition of "substantial interest".

This consistency should be extended to Policy. The Policy uses:

- "direct investment" for foreign government investor acquisitions (which is defined to include a 10% interest);
- "investment" in the media sector requirement;
- "interest" in the real estate requirements.

"Interest in" should be a consistent term.

BLS Recommendations:

- extend FATA s12B to specifically include "interest in a unit" in the definition of "interest in trust estate";
- replace the words "acquisition is of shares" at FATR 3(i) and 3(j) with "acquisition is of interests in shares";
- replace the words "acquisition is of units" at FATR 3(o) with "acquisition is of interests in units"; and
- use "interest" consistently in the Policy.

10. Update Form 1 (Notice under section 25) and Form 2 (Notice under section 26)

The versions of these forms available from the FIRB website are not consistent with the versions set out in the schedule to the Foreign Acquisitions and Takeovers (Notices) Regulations 1975 (Cth) (**FATNR**). Their formatting also makes them difficult to complete.

The forms are also out-of-date in that they request telex numbers but not email addresses and do not reflect legislative changes (e.g. references to "substantial shareholding" instead of "substantial interest", reference to Australian corporations being "incorporated" in a State, Territory instead of "registered" and no request for ACNs or ABNs).

These forms should be revised to bring them up-to-date and to better collect data of relevance to FIRB's consideration of an application. We have been made aware of a new online portal that is being trialled that will effectively replace the notices. However, these forms will still need to be updated in the FATNR.

BLS Recommendations:

- revise Forms 1 and 2 in the FATNR to bring them up-to-date and to better collect data of relevance to FIRB's consideration of an application.

11. 12 months approvals

The Policy states that "applications to acquire interests that will not be substantially completed within 12 months will generally not be accepted".

It would be helpful if the Policy could specify in general terms the circumstances in which FIRB may be prepared to give approvals which last for more than 12 months.

BLS Recommendations:

- provide in the Policy examples of circumstances in which FIRB may be prepared to give approvals which last for more than 12 months (e.g. exercise of share options).

SCHEDULE 2

FURTHER TECHNICAL ISSUES INVOLVING SWF's AND SOE's

1. *Exclude financial sponsors from the definition of foreign government investors*

The broad definition of foreign government investors inadvertently captures domestic and offshore private equity funds whose investors include SWFs and other state owned entities such as pension funds and state owned university investment funds which invest in private equity funds. In the United States of America (**US**) in particular, the level of ownership of these investors is often greater than 15% in any one fund (or more than 40% in aggregate by these types of investors).

Importantly, however, such investments are usually passive and none of the relevant government entities have any influence or control over the investment or operational decisions of the private equity fund. In the experience of BLS members the most common investment form is a limited liability partnership where the SWF investor holds passive limited partnership interests. It is the general partner of such an entity that exclusively makes investment decisions.

The BLS is concerned that the current regulation of foreign government investors is not targeted to address government policy concerns that there is a risk that such investments might not be commercial in nature or could be undertaken in pursuit of political or strategic objectives that may be contrary to Australia's national interest.

BLS Recommendations:

- exempt non-controlling investment by "commercial" funds such as private equity funds so that the thresholds are consistent with the general review thresholds.

2. *Clarify requirements for SOE acquisitions of interests in land*

The Policy states that "Foreign government investors must notify the Government and get prior approval to...acquire an interest in land."

The BLS understands that the Foreign Investment Review Board (**FIRB**) interprets "interest in land" with reference to the FATA s12A definition of "interest in Australian urban land" as though all references to "Australian urban land" in FATA s12A are taken also to refer to "Australian rural land". This should be clarified in the Policy.

The BLS also understands that FIRB takes the view that none of the exemptions for Australian urban land interest acquisitions in regulation 3 of the FATR apply to the Policy. This should be clarified in the Policy.

The BLS also understands that the acquisition by a foreign government investor of securities in an Australian urban land corporation or Australian urban land trust estate constitutes an acquisition of an "interest in land" for which prior approval is required under the Policy. It is unclear whether this means the acquisition of any securities or only the acquisition of securities which would constitute a "direct investment" (e.g. more than 10%). The BLS submits it should be the latter. The position should be clarified in the Policy.

BLS Recommendations:

- clarify the Policy that "interest in land" is defined with reference to the FATA s12A definition of "interest in Australian urban land" as though all references to "Australian urban land" in FATA s12A are taken also to refer to "Australian rural land";
- clarify the Policy that the FATR 3 exemptions for acquisitions of interests in Australian urban land do not apply to the Policy; and
- clarify the Policy so that only acquisitions of security interests over shares in an Australian urban land corporation or units in an Australian urban land trust estate which constitute a direct investment (10% or more) is subject to approval under the Policy.

3. *Provide more guidance as to what loans fall within SOE direct investment*

There is widespread confusion as to whether and to what extent a loan by a foreign government investor constitutes a "direct investment" requiring prior approval under the Policy. Further guidance on this issue is essential.

What the current Policy states in relation to loans is that:

- foreign government investors regulated by Australian Prudential Regulation Authority (**APRA**) do not need to obtain prior approval to obtain security as part of a lending agreement or to subsequently enforce the security and sell the assets (see footnote 2);
- however, APRA-regulated foreign government investors must obtain prior approval to gain control over a previously secured asset and to retain it for more than 12 months (see footnote 2);
- a foreign government investor must obtain prior approval to obtain an interest in an entity of less than 10% if that investor also extends a loan to the entity (see definition of "direct investment"); and
- a foreign government investor must obtain prior approval to retain an interest in an entity of 10% or more following enforcement of a security interest (see definition of "direct investment").

Given the Policy's focus on secured loans, the BLS assumes that approval is not required for unsecured loans. However, the Policy should confirm if this is the case, given that it is common for even unsecured loans to contain undertakings and covenants in favour of the lender which could be construed as providing the lender with "potential influence or control over the target" (see Policy's definition of "direct investment").

In terms of secured loans, the Policy should explain how, as a practical matter, FIRB applies the "direct investment" test. As a threshold matter a secured loan should only constitute a "direct investment" where security is being granted over 10% or more of the borrower's assets by book value.

There should also be clarification of how the 10% threshold applies in the case of a syndicated secured loan. The BLS understands it is with reference to a financier's participating interest in the loan. Consistent with the previous paragraph, a foreign government investor's participation in a secured syndicated loan should only constitute a "direct investment" where the participating interest is 10% or more and where security is being granted over 10% or more of the borrower's assets by book value.

BLS Recommendations:

- clarify the Policy that unsecured loans are not direct investments requiring prior approval;
- limit the definition of direct investment in the Policy to secured loans where security is being granted over 10% or more of the borrower's assets by book value;
- clarify the Policy that a foreign government investor's participation in a syndicated secured loan should only constitute a "direct investment" where the participating interest is 10% or more and where security is being granted over 10% or more of the borrower's assets by book value; and
- include a specific exemption for banks acting as security trustees.

4. Provide more guidance as to what equity investments fall within SOE direct investment

It would be helpful if the Policy could provide more guidance on what types of equity investments constitute "direct investments" requiring prior approval under the Policy.

In particular it is unclear as to how the following sentence is to be applied in situations other than those involving only acquisitions of issued shares or units in a single class: "Any investment of an *interest* of 10 per cent or more is considered to be a direct investment."

It would be preferable if the concept of "interest" is defined with reference to the definition of "substantial interest" at FATA s9. That is to say, a person is taken to have an "interest" of 10% or more in an entity if the person:

- has voting power of at least 10%;
- has potential voting power of at least 10%;
- holds interests in at least 10% of the entity's issued shares or units; or
- would hold interests in at least 10% of the entity's issued shares or units if shares or units were issued as a result of the exercise of convertible securities.

BLS Recommendations:

- define "interest" in the definition of "direct investment" and generally in the revised Policy with reference to the definition of "substantial interest" at FATA s9 (see above).

SCHEDULE 3

MODIFIED DEFINITION OF "ASSOCIATE" FROM BROADCASTING SERVICES ACT

For the purposes of this Act, "associate" means:

(a) *the person's spouse or a parent, child, brother or sister of the person; or*

(b) *a partner of the person or, if a partner of the person is a natural person, a spouse or a child of a partner of the person; or*

(c) *if the person or another person who is an associate of the person under another paragraph receives benefits or is capable of benefiting under a trust--the trustee of the trust; or*

(d) *a person (whether a company or not) who:*

(i) *acts, or is accustomed to act; or*

(ii) *under a contract or an arrangement or understanding (whether formal or informal) is intended or expected to act;*

in accordance with the directions, instructions or wishes of, or in concert with, the first-mentioned person or of the first-mentioned person and another person who is an associate of the first-mentioned person under another paragraph; or

(e) *if the person is a company--another company if:*

(i) *the other company is a related body corporate of the person for the purposes of the Corporations Act; or*

(ii) *the person, or the person and another person who is an associate of the person under another paragraph, are in a position to exercise control of the other company.*