Chapter 3

Administration of foreign investment in Australia

3.1 As suggested in the introduction to this report, foreign investment in Australia is regulated by the *Foreign Acquisitions and Takeovers Act 1975* (FATA). Under the act, the government has the power to block proposals which would result in a foreign person acquiring control of an Australian corporation or business or an interest in real estate where this is determined to be contrary to the 'national interest'. The Treasurer is responsible for administering the FATA. The FATA and the *Foreign Acquisitions and Takeovers Regulations 1989* provide monetary thresholds below which the relevant FATA provisions do not apply, and separate thresholds for acquisitions by U.S. investors. The FATA also provides a legislative mechanism for ensuring compliance with the policy.[1] The FATA is administered by the Foreign Investment Review Board (FIRB)—a non-statutory review body which was established in 1976.

3.2 Australia's foreign investment policy as articulated in Treasury's policy documents states:

> The Government's approach to foreign investment policy is to encourage foreign investment consistent with community interests. In recognition of the contribution that foreign investment has made and continues to make to the development of Australia, the general stance of policy is to welcome foreign investment. Foreign investment provides scope for higher rates of economic activity and employment than could be achieved from domestic levels of savings. Foreign direct investment also provides access to new technology, management skills and overseas markets.[2]

3.3 In giving evidence to the committee, Mr Patrick Colmer, FIRB/ Department of the Treasury, referred to the 'default position' contained within the legislation:

> The way that the legislation is set up is that the default position is that the investment is allowed to proceed. The legislation is set up so that it is clearly the exception rather than the rule to intervene in an investment case. What the legislation does is provide an opportunity for the Treasurer, as the responsible minister, to raise objections if a proposal is considered to be against the national interest.[3]

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1 Department of the Treasury, 'Australia's Foreign Investment Policy ' available at: http://www.firb.gov.au/content/_downloads/Australia's%20Foreign%20Investment%20Policy.pdf, p. 1 (accessed 21 May 2009).

2 The Treasury, 'Australia's Foreign Investment Policy' available at: http://www.firb.gov.au/content/_downloads/Australia's%20Foreign%20Investment%20Policy.pdf, p. 1 (accessed 21 May 2009).

3 *Committee Hansard*, 22 June 2009, p. 5.

3.4 All applications before the FIRB are examined on a case-by-case basis and as this comment suggests, the Treasurer can make determinations based on the national interest.[4]

History of foreign investment regulation in Australia

3.5 Listed below are some of the major landmarks in the development of Australia's foreign investment policy. Since the introduction of the *Foreign Acquisitions and Takeovers Act* in 1975, there has been an increasing liberalisation of Australia's foreign investment policy through:

- the introduction of higher thresholds, below which proposals do not require approval; and
- the progressive abolition of Australian equity and control requirements.

3.6 The *Foreign Acquisitions and Takeovers Act 1975* established a regime for screening takeovers and authorising proposals to establish new businesses, investments by foreign governments and real estate purchases. It was established to provide clarity on Australia's foreign investment policy and, at least in part, address fears about Japanese investment in Australia.[5]

3.7 In 1976 a further package of reforms was announced which included the establishment of FIRB to replace the existing committee of public servants with a three member panel, comprising two members with business sector experience and a senior Treasury official. The explanation for the change focused on the government's perceived need to obtain independent expert advice from persons who reflected community and business sector interests.[6]

3.8 In 1986 the test requiring applicants to demonstrate net economic benefits, and that Australians had had the opportunity to purchase the target business, was dropped. A new test was introduced which assessed whether a proposal for foreign investment was in the 'national interest'.[7] The national interest test is examined later in this chapter from paragraph 3.33.

3.9 From 1987, new monetary thresholds, below which the relevant FATA provisions do not apply, were introduced for foreign takeovers of less

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4 See The Treasury, 'Australia's Foreign Investment Policy' available at: http://www.firb.gov.au/content/_downloads/Australia's%20Foreign%20Investment%20Policy.pdf (accessed 21 May 2009), p. 2.

5 Senate Select Committee on Certain Aspects of Foreign Ownership Decisions in Relations to the Print Media, *Percentage Players: the 1991 and 1993 Fairfax Ownership Decisions*, June 1994, p. 179.

6 *Percentage Players*, June 1994, p. 179.

7 *Percentage Players*, June 1994, p. 179.

than $5 million.[8] (1987 was also significant as Hamersley Iron, now Rio Tinto, established a joint venture with China's Sinosteel (60/40) to develop the Channar iron ore deposit. This was China's first large-scale investment in Australia and remained China's most significant investment in Australia for many years.[9])

3.10 In 1993 the rule that 50 per cent Australian equity was required in a resource project—unless it could be demonstrated that that equity was not available—was abolished.[10]

3.11 In 1999 the threshold for which applications are registered but are generally not fully examined is raised from $50 million to $100 million.[11]

3.12 In 2008 Treasurer Wayne Swan announced new guidelines for assessing foreign investment by sovereign wealth funds and state-owned entities. These sought to clarify the government's position on foreign investment from state-owned entities. That guideline which relates most specifically to investment by SOEs states: 'In considering issues relating to independence, the Government will focus on the extent to which the prospective foreign investor operates at arm's length from the relevant government'.[12] These guidelines are available at Appendix 3.

Foreign Investment Review Board

Administrative structure

3.13 The FIRB is a non-statutory body, with a board of directors, who advise the Treasurer on the government's foreign investment policy and its administration. Current board members of the FIRB are: Mr John Phillips AO, Ms Lynn Wood, The Hon Chris Miles and Mr Patrick Colmer.[13] Mr Patrick Colmer, as the Executive Member of the Board and as the General Manager of the Foreign Investment and Trade Policy Division of the Department of the Treasury, provides the link between the Board and the Treasury. While the Board provides advice on the application of the

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8 CEDA, 'The contribution of foreign direct investment and the mining industry to the welfare of Australians', Information Paper No 92, November 2008, p. 15.

9 Australia China Business Council, *Committee Hansard*, 2 July 2009, p. 2.

10 Hence, most of the Japanese investments during the 1970s and 80s were less than 50 per cent holdings. Numerous witnesses spoke to the committee about this paradigm shift in foreign investment policy, see Mr Patrick Colmer, FIRB/ Treasury, *Committee Hansard*, 22 June 2009, p. 3 and Professor Peter Drysdale, *Committee Hansard*, 1 July 2009, p. 40.

11 Treasurer Peter Costello, 'Foreign Investment Policy Changes', 2 September 1999, http://www.treasurer.gov.au/DisplayDocs.aspx?pageID=&doc=pressreleases/1999/055.htm&min=phc (accessed 30 July 2009).

12 A submission from the Minerals Council of Australia suggests, these new guidelines 'represented an elaboration, rather than any significant amendment to the existing rules which are set out in the *Foreign Acquisitions and Takeovers Act 1975*', *Submission 57*, p. 4.

13 Biographical data on board members can be found in the *Annual Report 2007–08*, p. 4 or the FIRB website: http://www.firb.gov.au/content/who.asp?NavID=48 (accessed 29 April 2009).

policy across the range of proposals, much of the day to day administration associated with foreign investment applications is undertaken by Treasury staff within the Division. The Division also provides guidance to foreign investors, and where necessary, assists shape proposals to conform to the policy.[14]

FIRB's jurisdiction

3.14 As suggested above, the Foreign Investment Review Board is responsible for administering the *Foreign Acquisitions and Takeovers Act 1975*. The Board's functions are strictly advisory and it has no authority to approve or reject foreign investment applications. Responsibility for the policy, and for making decisions on foreign investment proposals, rests with the Treasurer.[15] The Treasurer does not have to accept the advice of FIRB, and makes determinations on a case-by-case basis according to an assessment of the national interest.[16]

3.15 The role of the Board, as outlined in its annual report, is to:

- Examine proposed investments in Australia that are subject to the policy and supporting legislation, and to make recommendations to the Treasurer on these proposals;
- Advise the Treasurer and other Treasury portfolio ministers on the operation of the policy and the *Foreign Acquisitions and Takeovers Act 1975* (the FATA), and on proposed investments that are subject to each;
- Foster an awareness and understanding, both in Australia and abroad, of the policy and the FATA;
- Provide guidance to foreign persons and their representatives/agents on the policy and the FATA; and
- Monitor and ensure compliance with the policy and the FATA.[17]

Administration of applications to the FIRB

3.16 At the Budget Estimates hearing of June 2009, Mr Patrick Colmer offered the following description of the way the review process works:

> The way that the system works is that applications for foreign investment approval are, in the first instance, assessed by Treasury in my division. My division provides secretariat services to the board as well as advice to the minister. Under the legislation, the Foreign Acquisitions and Takeovers

14 FIRB, *Annual Report 2007–08*, pp. 4–5.

15 FIRB, *Annual Report 2007–08*, pp. 3–4.

16 This was the case in 2001 when Treasurer Peter Costello rejected Shell Australia's proposed acquisition of Woodside Petroleum, Treasury website, http://www.treasury.gov.au/documents/178/HTML/docshell.asp?URL=ch3.asp (accessed 12 August 2009).

17 FIRB, *Annual Report 2007–08*, p. 3.

> Act, the Treasurer is the minister who is required to make a decision on each case. The Treasurer does that with a combination of advice from the Foreign Investment Review Board and the Treasury as his department. It varies depending on the nature of the case and the size and similar sorts of things, but typically we consult confidentially with other relevant government departments, we do our own analysis of the particular issues that might arise in a particular case, and then depending on the significance of the case and what sort of issues might appear, the Foreign Investment Review Board will have a varying degree of involvement. The Foreign Investment Review Board itself does not look at the routine cases; it only looks at the more significant cases and that provides [confidential] advice to the minister via the department.[18]

3.17 Mr Colmer also made it clear that the Treasurer does not approve each 'significant case' but rather he has the opportunity to raise objections about an application within the statutory period:

> The way the legislation is set up all that it requires at its simplest level is for people who are proposing an investment to make a notification. Under the legislation there is then a statutory period, which is usually 30 days but can be extended, during which the Treasurer may raise objections. If the Treasurer does not raise objections, at the conclusion of that statutory period there is no further capacity for the government to intervene. It is an important distinction…but the government does not approve foreign investment proposals. If they are concerned about a foreign investment proposal the minister needs to take a positive step to raise an objection. That is what the legislation does. The minister can object outright or apply conditions to mitigate the national interest in each case.[19]

3.18 In 2007–08, 7,841 proposals received foreign investment approval under Australia's foreign investment policy and the *Foreign Acquisitions and Takeovers Act 1975*. This compares with 6,157 the previous year, representing an increase of 27 per cent. The real estate sector recorded 7,357 approvals (31 per cent higher than the 5,614 approvals in 2006–07). There were 484 proposals approved in other sectors in 2007–08 compared with 543 in 2006–07, a decrease of 11 per cent.[20]

3.19 In 2007–08, one proposal was rejected by the way of a Final Order, compared with 27 in 2006–07. There were no Divestiture Orders made in 2007–08, (compared with none in 2006–07 and five in 2005–06). There were 13 Interim Orders (90 in 2006–07), extending the 30-day statutory decision making period by up to 90 days.[21]

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18 *Committee Hansard*, Senate Economics Legislation Committee, *Budget Estimates*, 4 June 2009, p. 13.

19 *Committee Hansard*, Senate Economics Legislation Committee, *Budget Estimates*, 4 June 2009, p. 57.

20 FIRB, *Annual Report 2007–08*, p. xv.

21 FIRB, *Annual Report 2007–08*, p. xv; FIRB, *Annual Report 2006–07*, p. xv.

3.20 Approvals in 2007–08 involved proposed investment of $191.9 billion. This represented a 22 per cent increase on the previous year's approvals of $156.4 billion (while, for the previous reporting period, the figure was $87 billion).[22]

Applications considered 2002–03 to 2007–08—number of proposals[23]

Outcome	2002–03	2003–04	2004–05	2005–06	2006–07	2007–08
Approved unconditionally	1,105	995	1,127	1,386	1,520	1,656
Approved with conditions	3,562	3,452	3,233	3,800	4,637	6,185
Total approved	4,667	4,447	4,360	5,186	6,157	7,841
Rejected	80	64	55	37	39	14

3.21 As noted in the previous chapter, while these figures are indicative of broader trends, they do not incorporate applications made after 1 July 2008. It should also be noted that the majority of foreign investment proposals involve the purchase of real estate. Of the 7,841 applications which were considered during 2007–08, more than 7,000 were real estate applications. However, despite the differences in numbers of applications, non-real estate applications were worth considerably more than those for real estate.[24]

Total approvals by industry sector in 2007–2008—proposed investment value[25]

Mineral exploration and development	33%
Real estate	24%
Services	19 %
Manufacturing	16%
Finance and insurance	5%
Tourism	2%
Agriculture, forestry and fishing	1%
Resource processing	Less than 0.5%

22 FIRB, *Annual Report 2007–08*, p. xv; FIRB, *Annual Report 2006–07*, p. xv.

23 Adapted from, FIRB, *Annual Report 2007–08*, p. 20.

24 For a more complete breakdown in figures see FIRB, *Annual Report 2007–08*, p. 22.

25 Adapted from FIRB, *Annual Report 2007–08*, p. 27.

Rejected applications

3.22 At Budget Estimates, June 2009, Treasury officials were asked the number of business case deals (rather than real estate applications) that have been recently rejected by the Treasurer. Mr Colmer responded that none had been rejected by the current Treasurer and that one—Shell Australia's proposed acquisition of Woodside Petroleum in 2001—was rejected by the previous Treasurer.[26] In total, 16 had been rejected since 1990.[27] In appearing before the committee for the purposes of this inquiry, Mr Colmer went further explaining:

> If you look back at the cases that we have rejected, you can see that we have not rejected outright very many at all. In fact our best information is that 16 cases have been rejected since 1990. That is out of something in the order of, on average, about 500 business cases a year. We have had a different pattern in real estate but I have not actually been talking about that. The predominant reason for rejecting those cases has been to do with various forms of criminality on the part of the proposer. There is also the Shell-Woodside case where the decision was taken back in 2001 that Shell was not going to develop that resource; and the decision was taken at the time that the national interest was best served by developing that resource much more quickly than Shell was expected to do it.[28]

Monetary thresholds and determining substantial interest

3.23 The FATA and the *Foreign Acquisitions and Takeovers Regulations 1989* provide monetary thresholds below which the relevant FATA provisions do not apply, and separate thresholds for acquisitions by U.S. investors.[29]

3.24 The FATA empowers the Treasurer to examine proposals by foreign persons who seek to:

- acquire, or to increase, a substantial shareholding in, or acquire a controlling interest in the assets of, a prescribed Australian corporation valued above the relevant thresholds; or
- acquire an interest in Australian urban land.[30]

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26 This proposal was rejected on national interest grounds. The then treasurer, Peter Costello, was of the view that if approved Shell may not give preference to developing the North West Shelf project to its maximum potential, see http://www.treasurer.gov.au/DisplayDocs.aspx?pageID=&doc=pressreleases/2001/025.htm&min=phc (accessed 31 July 2009).

27 *Committee Hansard*, Senate Economics Legislation Committee, Budget Estimates, 4 June 2009, p. 55.

28 *Committee Hansard*, 22 June 2009, p. 6.

29 Australia's Foreign Investment Policy, http://www.firb.gov.au/content/_downloads/Australia's%20Foreign%20Investment%20Policy.pdf (accessed August 12 2009).

30 FIRB, *Annual Report 2007–08*, p. 45.

3.25 A substantial interest therefore is where a person, alone or together with any associate(s), is in a position to control not less than 15 per cent of the voting power or holds interests in not less than 15 per cent of the issued shares of a corporation.[31]

3.26 Currently, under the FATA, the threshold is total assets which amount to $100 million or more.

3.27 In August 2009 the Treasurer announced additional reforms to Australia's foreign investment policy (with the amended regulations to be introduced in September 2009). These reforms, which represent a significant liberalisation of foreign investment policy, would see the threshold for reviewable applications adjusted from $100 million to $219 million. Accordingly, individual investments above 15 percent of a target company that are worth less than $219 million will no longer require FIRB examination. The effect of the changes is that approximately 20 per cent of all business applications will no longer be screened by FIRB.[32] It is also proposed that the some of the thresholds will be indexed annually against the GDP deflator. The summary of measures announced is included in the following table.[33]

Current Thresholds	Proposed Thresholds
Foreign Investor—Interest in an Australian business $100 million (not indexed)	$219 million (ALL indexed on 1 January each year to the GDP price deflator in the Australian National Accounts for the previous year)
Foreign Investor—Offshore Takeover $200 million (not indexed)	
US investors only—Sensitive sector acquisition $110 million (indexed)	
US Investors only—Offshore Takeover $219 million (indexed)	
US Investors only—Interest in an Australian business $953 million (indexed).	$953 million (indexed on 1 January each year to the GDP price deflator in the Australian National Accounts for the previous year)
Foreign Investor—establishing a new business $10 million (not indexed)	Abolished

31 An aggregate substantial interest is where two or more persons together with any associate(s), are in a position to control not less than 40 per cent of the voting power or hold interests in not less than 40 per cent of the issued shares, of a corporation. FIRB, *Annual Report 2007–08*, p. 45.

32 Treasurer Wayne Swan, 'Reforming Australia's foreign investment framework', http://www.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2009/088.htm&pageID=003&min=wms&Year=&DocType= (accessed 12 August 2009).

33 Treasurer Wayne Swan, 'Reforming Australia's foreign investment framework', http://www.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2009/088.htm&pageID=003&min=wms&Year=&DocType= (accessed 12 August 2009).

3.28 As this table indicates, the thresholds of investments from the United States are higher than they are for citizens/ corporations investing from other nations.

Structuring applications to avoid review

3.29 During public hearings Senator Barnaby Joyce frequently identified concerns he had with companies structuring multiple bids in a way that avoids meeting the threshold that triggers government review. When the committee was in Brisbane Sentor Joyce stated:

> You go piece by piece by piece so that you never trigger the guidelines. Also they could separate it into different companies—Chinalco buys that and Shenhua buys that and—surprise, surprise—none of them is over $100 million.

3.30 Senator Joyce went on to question whether there should be a related entity test in the Foreign Investment Review Board guidelines that says:

> You're all part of the government of the People's Republic of China so, if you are buying land in Australia, we are going to add it all up into a bundle. That can be a trigger. If it adds up to more than $100 million we will look at it en globo?[34]

3.31 When asked about whether parties may manipulate the process through reducing their total ownership to below 15 per cent while still assuming more than 50 per cent of a strategic asset, Mr Patrick Colmer, suggested that the legislation still required tightening:

> The way that the legislation is written says that a 15 per cent interest in either the issued shares or the voting power of the company is the trigger. That is the way that the law is written. That is the way it has been since 1975. Yes, it is possible to construct a proposal that may not trigger that. It is one of the reasons why the government announced that we would be looking at a legislative fix on that.[35]

Committee view

3.32 The committee notes that the legislation identifies that a substantial interest refers to an instance where a person, alone or together with any associate(s), is in a position to control not less than 15 per cent of the voting power or holds interests in not less than 15 per cent of the issued shares of a corporation.[36] The committee also notes Mr Colmer's comment that it is possible to structure a proposal so that total

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34 *Committee Hansard*, 1 July 2009, pp. 8–9.

35 *Committee Hansard*, 22 June 2009, pp. 11–12.

36 An aggregate substantial interest is where two or more persons together with any associate(s), are in a position to control not less than 40 per cent of the voting power or hold interests in not less than 40 per cent of the issued shares, of a corporation. FIRB, *Annual Report 2007–08*, p. 45.

ownership is below 15 per cent while component parts of the application may be for more than 15 per cent of a strategic asset—something which Mr Colmer explains that the government is reviewing.

Recommendation 3

3.33 The committee recommends that the government tighten the FATA legislation to deal with complex acquisitions where takeovers of smaller strategic assets may be masked by an application which, in total, does not represent more than 15 per cent, and therefore does not trigger review. The committee would like FIRB to give adequate consideration to the interaction between the various components of an acquisition.

National interest test and case-by-case assessment

3.34 The FATA empowers the Treasurer to prohibit an acquisition if he/she is satisfied that the acquisition would be 'contrary to the national interest'. However, the national interest, and hence what would be contrary to it, is not defined in the FATA. Given the important role foreign investment has played in Australia's national development—and the default position of FIRB—it would appear that there is a general presumption that foreign investment proposals will generally serve the national interest.[37]

3.35 Additional guidance on aspects of the national interest include, for example:

- Existing whole-of-government policy and law—reflecting the view that existing policy and law define important aspects of the national interest (for example, telecommunications, media, aviation, environmental regulation and competition policy);
- National security interests; and
- Economic development.[38]

A proposal that does not meet the requirements set out in the policy would be regarded as being contrary to the national interest.

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37 For a full description of the 'national interest' criteria see the *FIRB Annual Report 2006–07*, pp 7–8, http://www.firb.gov.au/content/Publications/AnnualReports/2006-2007/_downloads/2006-07_FIRB_AR.pdf (accessed 15 May). In evidence provided to the committee at Senate Estimates, Treasury official Mr Jim Murphy suggested: 'The "national interest" prior to this government has been a term which, to some extent, has been criticised because it was not clear what a government would take into account in terms of the national interest. This government put forward those principles or guidelines to give some guidance to people who are making foreign investment proposals as to the types of things the government would take account of. They do not limit the government in terms of what it can take account of as to what is in the national interest. *Committee Hansard*, Senate Economics Legislation Committee, Budget Estimates, 4 June 2009, p. 56.

38 FIRB, *Annual Report 2006–07*, p. 8.

3.36 In responding to questions about the how the national interest is defined, Mr Colmer suggested:

> But if you look at what elements might make up a national interest concern, then I think you cannot do better than to go back to the Treasurer's statement of February last year where he announced the principles for foreign government investments. As I am sure you are aware, there were six principles that were laid out there—only one of which is specifically relevant to state owned enterprises. The other five are considerations that we take into account on any proposal. They are things like competition impacts, the taxation implications, national security considerations, the impact on other Australian businesses and how well a company can be expected to operate within the Australian system.[39]

3.37 Treasury documents also identify the way that the test operates as a 'negative' rather than a 'positive' test:

> Although the existence of a national interest test may appear to be non-transparent, it is a negative test rather than a prescriptive test to a list of criteria. The onus is on the Australian authorities to have reason to reject a proposal, rather than on the investor to show benefits to Australia, and the reasons for rejection are always made known to the investor.[40]

3.38 Many submitters to the inquiry agreed that defence and security industries (and/or sites) should be quarantined from foreign ownership or control. Further that, in such instances, the national interest test had clear application. However, others argued that beyond the security sphere the notion of the national interest is vague and insufficiently defined. The IPA argued that the national interest test is 'opaque' and 'nebulous' and that the Treasurer can deny entry to any significant foreign investor 'in the national interest' without legal constraints or transparent explanation.[41] Professor Tony Makin claims that the national interest has not been adequately defined and that it is 'devoid of any economic meaning'.[42]

3.39 Others saw benefits in the national interest test. Professor Peter Drysdale claimed, '…the national interest test encompasses all the relevant factors that you need to apply in the consideration of foreign investment proposals in Australia'.[43] While Mr

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39 *Committee Hansard*, 22 June 2009, p. 6.

40 Department of the Treasury, 'Foreign Direct Investment Policy', http://www.treasury.gov.au/documents/178/HTML/docshell.asp?URL=ch3.asp (accessed 14 August 2009).

41 *Submission 32*, pages 4, 11, 14.

42 Professor Tony Makin, 'Capital xenophobia and the national interest', Australia's Open Investment Future, Institute of Public Affairs, Melbourne, 4 December 2008, p. 1.

43 *Committee Hansard*, 1 July 2009 p. 32. In relation to Chinese investment in the minerals sector, Professor Drysdale and Professor Findlay claimed 'there are no issues that cannot be dealt with under the umbrella test of national interest in managing the growth in Chinese FDI into the Australian minerals sector', *Submission 40*, p. 1.

Julian Tapp, Fortescue Metals Group, suggested 'In our view it (the national interest test) worked very well…We looked at it and we thought it was an eminently sensible test'.[44]

3.40 Rio Tinto identified the importance of a having a flexible system through which applications would be assessed on a case-by-case basis:

> The flexibility of the structure that we have in Australia to be able to look at it on a case-by-case basis does allow for appropriate consideration to be given to factors in the particular circumstances of that particular case. A hard and fast application of a rules based process would risk coming up with the wrong policy results.[45]

3.41 This approach was also supported by the Australia China Business Council who argued: 'The fact that the current FIRB rules are structured to address individual applications on a case-by-case basis is the correct approach, and it has served Australia well'.[46]

Committee view

3.42 The committee considers that the chief virtue of the national interest test is its flexibility. Its unwritten or undefined character—the fact that it is a negative test—enables it to adapt more easily to changing circumstance. A prescriptive test with specific criteria would not allow this degree of flexibility. The committee also believes that the national interest test should continue to focus on the commercial use of an asset and not upon its ownership.

Timeframes for review

3.43 Under the FATA, the Treasurer has 30 days to review investments, a 10-day notice period and a mechanism for a 90-day interim order extension (that is made public) if considered necessary.

3.44 Some concerns were expressed to the committee about the length of time it can take FIRB to review applications. In identifying concerns related to timeframes for review the Australian China Business Council (ACBC) identified the application made by Chinese steel producer Angang Steel for a minority shareholding in Gindalbie:

> …there has been a lot of concern about the time frame taken over decision making and delays. For example, one of the more vanilla investments into Australia was Angang's minority shareholding into Gindalbie, which took six months to get approval and which seems very difficult to understand. By contrast, the time taken by the government to consider the Chinalco bid

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44 *Committee Hansard*, 2 July 2009, p. 29.

45 *Committee Hansard*, 1 July 2009, pp. 46–47.

46 *Committee Hansard*, 2 July 2009, p. 4.

> for Rio does not appear to be unreasonable because that is a very major and significant transaction for Australia involving existing mature assets, not just greenfield developing projects. But I think that issue of delay and the lack of accountability does create concerns overseas that different countries get treated differently.[47]

3.45 The ACBC recommended reviewing the time taken to make decisions under the FATA.[48] Rio Tinto reinforced that timely responses were imperative, particularly when large capital transactions were involved:

> Clear and prompt decision making by government is critical in demonstrating that Australia is welcoming of foreign investment. In undertaking major capital transactions, time is of the essence.[49]

3.46 In their evidence to the committee, Fortescue Metals explained with reference to Hunan Valin's $650 million application for a 17.55 per cent share of Fortescue, that they would 'have liked the approval in a faster time frame' but felt that FIRB 'acted quickly in terms of their frame of reference'. Mr Tapp went on to explain, 'It took longer than 30 days to get the approval through. I think it would have been around 40 to 45 days'.[50]

Applying conditions to approvals

3.47 As noted above, conditions can be applied to foreign investment applications. At the time of writing, there have been three statements by the Treasurer during 2009 on substantial commercial cases where he has announced his approval with conditions attached. Each related to an application from a Chinese SOE.[51]

3.48 These relate to the following approvals:

- The Ashan Iron and Steel Group's application to acquire an additional shareholding in Gindalbie Metals up to a maximum of 36.28 percent.[52]
- Minmetals Non-ferrous Metals Company application to acquire certain mining assets of OZ Minerals.[53]
- Hunan Valin Iron and Steel Group for up to a 17.55 per cent shareholding in the Fortescue Metals Group (as outlined below).[54]

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47 *Committee Hansard*, 2 July 2009, pp. 6–7.

48 *Committee Hansard*, 2 July 2009, p. 3.

49 *Committee Hansard*, 1 July 2009, p. 44.

50 *Committee Hansard*, 2 July 2009, p. 30.

51 See FIRB website, 'Publications', http://www.firb.gov.au/content/publications.asp?NavID=5 (accessed 14 August 2009).

52 FIRB website, 'Foreign Investment Decision', 8 May 2009, http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2009/045.htm&pageID=003&min=wms&Year=&DocType=0 (accessed 14 August 2009).

53 FIRB website, 'Foreign Investment Decision', 23 April 2009, (accessed 14 August 2009).

Fortescue Metals Group and Hunan Valin

3.49 On 31 March 2009, the Treasurer approved the application of the Hunan Valin Iron and Steel Group for up to a 17.55 per cent shareholding in the Fortescue Metals Group. Under the proposal, Fortescue agreed to issue new shares to Hunan Valin to raise $650 million in funds for the next phase of its iron ore mining operations in the Pilbara.

3.50 The approval was subject to formal undertakings from both Hunan Valin and Fortescue. Those undertakings are as follows:

- Any person nominated by Hunan Valin to Fortescue's board will comply with the Directors' Code of Conduct maintained by Fortescue;
- Any person nominated by Hunan Valin to Fortescue's board will submit a standing notice under the *Corporations Act 2001* of their potential conflict of interest relating to Fortescue's marketing, sales, customer profiles, price setting and cost structures for pricing and shipping; and
- Hunan Valin and any person nominated by it to Fortescue's board will comply with the information segregation arrangements agreed between Fortescue and Hunan Valin.

Hunan Valin has also been asked to report to the FIRB on its compliance with these undertakings.[55] The Treasurer's announcement approving the deal states:

> Penalties for non-compliance with these undertakings are contained in the *Corporations Act 2001* and breaches of the Code of Conduct can lead to the director's removal from the company board.[56]

3.51 There are further enforcement provisions in the FATA. According to the act, if the Treasurer raises no objections to a proposal, subject to conditions, and the parties do not comply with the conditions, they may commit an offence under subsection 25(1C) of the FATA. Failure to comply with an order made by the Treasurer constitutes an offence under Section 30. The FATA empowers the Treasurer to make orders to prohibit schemes entered into for the purpose of avoiding its provisions (Section 38A). In addition, the provision of false or misleading information can constitute an offence under the Crimes Act 1914 and Chapter 7 of the Criminal Code Act 1995.[57]

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54 FIRB website, 'Foreign Investment Decision', 31 March 2009, (accessed 14 August 2009).

55 Treasurer Wayne Swan, Press Release, 'Foreign Investment Decision', 31 March 2009, http://www.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2009/032.htm&pageID=003&min=wms&Year=&DocType=0 (accessed 24 June 2009).

56 Treasurer Wayne Swan, Press Release, 'Foreign Investment Decision', 31 March 2009, http://www.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2009/032.htm&pageID=003&min=wms&Year=&DocType=0 (accessed 24 June 2009).

57 FIRB, *Annual Report 2007–08*, p. 49.

Other frameworks for regulating foreign investment

3.52 Beyond the *Foreign Acquisitions and Takeovers Act 1975*, Australia has a series of other regulatory frameworks to ensure that foreign investment in Australia operates lawfully and in the national interest. This is maintained through administrative bodies like the ACCC, and through legislation like the *Trade Practices Act*. In addition, work place and environmental standards are maintained through a range of separate regulatory entities.

Trade Practices Act

3.53 The purpose of the *Trade Practices Act 1974* is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection. The Act deals with almost all aspects of the marketplace: the relationships between suppliers, wholesalers, retailers, competitors and customers. In broad terms, the Act covers unfair market practices, industry codes, mergers and acquisitions of companies, product safety, product labelling, price monitoring, and the regulation of industries such as telecommunications, gas, electricity and airports.[58]

ACCC

3.54 The Australian Competition and Consumer Commission (ACCC) is an independent statutory authority that deals with competition law and anticompetitive practices. Formed in 1995 to administer the *Trade Practices Act 1974* and other relevant acts, the ACCC differs from that of the FIRB in so far as it does not have any role in relation to the *Foreign Acquisitions and Takeovers Act 1975*. Rather, they are the body responsible for evaluating the effect of foreign investment on competition. In evidence provided to the committee the ACCC explained:

> Our role in relation to acquisitions is restricted to purely competition assessment under section 50 of the Trade Practices Act, which prohibits, in effect, anticompetitive mergers…Of the, say, 400 mergers that we review each year, a fair number are actually referred to us by the Foreign Investment Review Board, and we will often conduct assessments in relation to those.
>
> Under section 50(3) the commission must have regard to a number of factors in assessing whether or not there is a breach of section 50. In that subsection the commission must have regard to things like input competition, concentration, barriers to entry, the likelihood of the removal of a vigorous and effective competitor, degree of substitutability and a few others.[59]

58 ACCC website: http://www.accc.gov.au/content/index.phtml/itemId/54137 (accessed 28 April 2009).

59 *Committee Hansard*, 22 June 2009, pages 14, 18.

3.55 Section 50 prohibits mergers and acquisitions that would be likely to have the effect of substantially lessening competition in a market in Australia. In assessing whether a merger or acquisition will contravene Section 50, the ACCC may only have regard to matters that have an effect on competition. Section 50(3) of the act sets out the factors that the ACCC must take into account in assessing the competition effects of a proposed acquisition. As suggested in the above evidence, no other factor other than those that relate to competition may be considered.[60] The ACCC also provided explanation on how they access proposed acquisitions in the mining sector:

> For acquisitions in the mining sector, there are two particular theories of competitive harm that we will examine when we are looking at a merger in terms of our assessment of whether or not there is a breach of section 50 of the Trade Practices Act. We are looking at the likely effect on competition, and there are several different types of theory of competitive harm that we will explore to see whether there is an anticompetitive effect. On the one hand, we will look at any horizontal aggregation of interests that the acquirer might already hold in addition to its acquisitions. For instance, if an acquirer already has some interests in Australia that compete with the target that it is intending to acquire, then we will look at the extent to which there might be some chilling or a diminution of competition in the market as a result of that acquisition. Separately—and this was an issue we explored particularly in the mooted Chinalco acquisition of Rio Tinto—we look at the vertical relationship as well, where you have an acquirer who does not necessarily have an interest that competes with its target head-to-head but it is a purchaser or has a related entity that is a purchaser of the product—the ore, for example—that is being produced by the target it is acquiring. The theory of harm we will examine there is the extent to which there can be any foreclosure of competitors through the vertical integration that might result or ensue from that acquisition. So they are two different anticompetitive effects that we will examine when we are looking at mergers generally and some of the acquisitions of mining interests in particular.[61]

3.56 In March 2009, the ACCC concluded, that on the basis of information provided to it during its review of the proposed Chinalco acquisition of a part of Rio Tinto, the acquisition was unlikely to substantially lessen competition under section

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60 ACCC, Public Competition Assessment, Chinalco (Aluminium Corporation of China)– proposed acquisition of interests in Rio Tinto plc and Rio Tinto Ltd, 25 March 2009, http://www.accc.gov.au/content/item.phtml?itemId=866062&nodeId=682aa011d83ba73fa9794e6cd75a75e3&fn=Chinalco%20(Aluminium%20Corporation%20of%20China)%20-%20proposed%20acquisition%20of%20interests%20in%20Rio%20Tinto%20and%20Rio%20Tinto%20Ltd%20-%2025%20March%202009%20-%20Mining%20.pdf (accessed 15 June 2009).

61 *Committee Hansard*, 22 June 2009, pp. 14-15.

50 of the Trade Practices Act and was unlikely to have the ability to unilaterally decrease global iron ore prices below competitive levels.[62]

Taxation

3.57 Concerns have been raised that companies who are partly foreign owned may become involved in transfer pricing arrangements—the pricing of assets, services and funds transferred within an organisation.[63] The transfer price will affect the allocation of the total profit among the parts of the company and may also be used to reduce taxable profits. The ATO examines transfer pricing arrangements for all companies operating in Australia.

Australian Stock Exchange

3.58 The Australian Stock Exchange can also provide a mechanism to protect against undue influence of foreign investors, including disclosure and corporate governance measures which ensure transparency and accountability. In its submission the Institute of Public Affairs argued:

> …the Australian government maintains the right to appropriately regulate where there may be a perceived risk from an external…investor. For example, the government can do so by ensuring that the standards of corporate governance for firms listed on the Australian Stock Exchange are rigorous and prevent large controlling shareholders from looting the firm's assets or expropriating firm value from minority shareholders. Given appropriate corporate governance standards, large controlling shareholders need not pose any investment threat or any other type of threat to Australia. With appropriate shareholder protection all investment would be in the national interest.[64]

Restrictiveness of Australia's foreign investment regime

3.59 Some submitters to the inquiry suggested that Australia needs to provide a regulatory environment that encourages foreign investment and that this could be achieved through easing its regulatory restrictions. Julie Novak, Institute of Public Affairs, argued Australia's foreign investment regulations were too restrictive and that if Australia is to attract more foreign capital it needs to relax its regulatory frameworks.[65] Dr Brian Fisher, Concept Economics, suggested that there are 'potential

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62 ACCC, Public Competition Assessment, Chinalco (Aluminium Corporation of China)– proposed acquisition of interests in Rio Tinto plc and Rio Tinto Ltd, 25 March 2009, (accessed 15 June 2009).

63 For example, *Submission 47*, p. 42.

64 *Submission 32*, p. 2.

65 *Committee Hansard*, 23 June 2009, p. 4. In relation to Chinese investment, Professor Peter Drysdale also cautioned '…if we deny ourselves the opportunity of hosting Chinese investment here, it will go elsewhere', *Committee Hansard*, 1 July 2009, p. 34.

deterrents in the current regime', while Rio Tinto also cautioned about having too much regulatory 'red tape', particularly for government-owned investors:

> …it is crucial that these principles (for assessing foreign investment proposals) be applied in a way that creates a foreign investment regime that will be sustainable in a period where more capital flows are likely to come from government owned investors. The fact is that investment capital will go elsewhere, particularly in the resources sector, if it is too difficult to do so in Australia. This means that the Australian economy will miss out on growth opportunities and that Australian businesses will lose market share to global competitors. This has occurred in the past, resulting in the creation of substantial competitors to Australian iron ore, in the case of Brazil, and coking coal, in the case of Canada, and at great cost to Australia.[66]

3.60 It would appear that, to some extent, this is a view shared by the Australian government. The Treasurer's statement on 4 August 2009, announcing reforms to Australia's foreign investment framework, made it clear that the government wanted to reduce disincentives to foreign investment:

> These reforms will help boost Australia's growth as the global economy recovers—streamlining Australia's foreign investment regime, cutting red tape and compliance costs, and improving Australia's competitiveness as a place to invest.[67]

3.61 This announcement clearly seeks to position Australia, during a time of capital scarcity, as an attractive and competitive destination for foreign investment.

3.62 Numerous submitters to the inquiry cited studies undertaken by the OECD, which suggest that Australia rates high in the OECD's 'regulatory restrictiveness index'. Julie Novak argued:

> I do not think there is too much doubt that Australia's regulatory regime is more restrictive than those of other countries, particularly those of continental Europe. One has to recognise that, for example, in continental Europe they have a free trade and investment zone, so, yes, that is a caveat. I think that the OECD investment restrictiveness index is reasonably credible. They have developed this index for a period of 10 years. Interestingly enough, it happens to be a by-product of Australian work in the late 1990s on investment in the services industry.[68]

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66 *Proof Committee Hansard*, 10 August 2009, p. 32; *Committee Hansard*, 1 July 2009, pp. 44–45.

67 Treasurer Wayne Swan, 'Reforming Australia's Foreign Investment Framework', 4 August 2009, http://www.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2009/089.htm&pageID=003&min=wms&Year=&DocType= (accessed 17 August 2009).

68 *Committee Hansard*, 23 June 2009, p. 3.

3.63 It is most likely that the recent decision to raise reviewable thresholds to $219 million will reduce Australia's high-end score on the OECD index.[69]

3.64 Others suggested that Australia's foreign investment framework was not sufficiently restrictive. Mr Ian Melrose argued that it is rare for FIRB to 'knock anything back' and there needs to be review of the board's 'parameters, direction and its ability to act in Australia's long-term interests'.[70] By comparison, the Farmers from the Liverpool Plans suggested lowering thresholds for mandatory FIRB assessment below $100 million.[71]

Recommendations from the *Percentage Players* report

3.65 The 1994 report by the Senate Select Committee on Certain Aspects of Foreign Ownership Decisions in Relations to the Print Media, recommends that the FIRB be replaced by an independent statutory authority to be known as the Foreign Investment Commission (FIC). The report also claims, citing a statement made by Treasurer the Hon Phillip Lynch in 1976, that it was originally envisaged that FIRB would eventually become a statutory body.[72] Making FIRB a statutory body would increase its decision making power and give it a higher degree of independence in foreign investment decisions.

3.66 Under the model proposed in the *Percentage Players* report the Treasurer would still make decisions on difficult or sensitive applications:

> (The) FIC would assume responsibility for administering foreign investment policies; making decisions on applications in non-key sectors; and referring proposals involving key sectors to the Treasurer accompanied by recommendations which would be made public.[73]

3.67 This recommendation was made because under the majority of foreign investment applications do not have national interest implications and could therefore

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69 The committee took limited evidence on the way Australia's foreign investment regulations compare with those of other nations. Mr Colmer suggested that, in a very general sense, Australia has a similar system to Canada, New Zealand and the United States. He suggested, 'There are quite different arrangements at the detailed level, but they are generally similar types of systems': The United States has a system called the Committee on Foreign Investment in the United States, generally referred to as CFIUS, and that is similar to the foreign investment process that we run. I would say, though, that our system is much more interventionist than the United States system…' *Committee Hansard*, 22 June 2009, p. 10.

70 *Proof Committee Hansard*, 10 August 2009, p. 25.

71 *Committee Hansard*, 1 July 2009, p. 8.

72 Statement to House of Representative 1 April 1976, Senate Select Committee on Certain Aspects of Foreign Ownership Decisions in Relations to the Print Media, *Percentage Players: the 1991 and 1993 Fairfax Ownership Decisions*, June 1994, Recommendation 10.8, p. 232.

73 Senate Select Committee on Certain Aspects of Foreign Ownership Decisions in Relations to the Print Media, *Percentage Players: the 1991 and 1993 Fairfax Ownership Decisions*, June 1994, Recommendation 10.8, p. 232.

be handled by an independent statutory body. The report adds that there would 'need to be a clear delineation between the powers of decision-making vested in FIC and those which would remain with the Treasurer' and that the new legislation would need to identify those classes of decisions to be made by the FIC.[74]

Committee view

3.68 As a non-statutory body FIRB's powers are formed under the government's common law or prerogative powers. However, because it is an advisory body, FIRB does not have effective or determinative power.

3.69 The committee can see possible advantages in FIRB being made a statutory body. This higher level of independence would allow decisions on foreign investment to operate at arm's length from government and this may assist depoliticise decision making on foreign investment. However, the committee is concerned about the implications this would have for the national interest test.

3.70 Under Australia's current system the power to decide upon the national interest is entrusted to an elected representative, in this case, the Treasurer. The committee believe that, in keeping with systems of delegated power in a Westminster system, an elected representative should continue to be ultimately responsible for determining the national interest.

3.71 The committee agrees with the proposal in the *Percentage Players* report, which suggest that it may be possible to establish a system whereby the new statutory authority makes the majority of decisions and sensitive 'national interest' cases continue to be referred to the Treasurer. However, the committee feels that such a system would not deliver outcomes much different to what we have under the current system and establishing a new system would only result in administrative duplication.

74 Senate Select Committee on Certain Aspects of Foreign Ownership Decisions in Relations to the Print Media, *Percentage Players: the 1991 and 1993 Fairfax Ownership Decisions*, June 1994, Recommendation 10.8, p. 234.