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Online Submission

Dear Sir/Madam

Submission on draft Foreign Acquisitions and Takeovers Legislation Amendment Bill 2015 and draft Foreign Acquisitions and Takeovers Regulations 2015

Herbert Smith Freehills is pleased to provide this submission in response to the Government's proposed reforms to Australia's foreign investment regime under the *Foreign Acquisitions and Takeovers Legislation Amendment Bill 2015* (**Draft Bill**) and *Foreign Acquisitions and Takeovers Regulations 2015* (**Draft Regulations**) (together, the **Proposed Legislation**).

This submission is based on our previous submissions in relation to:

- the consultation paper entitled 'Strengthening Australia's Foreign Investment Framework', submitted on 20 March 2015; and
- the consultation paper entitled 'Australia's Foreign Investment Framework: Modernisation Options', submitted on 29 May 2015,

(together our **Previous Submissions**),

and provides comments specifically in relation to the Proposed Legislation.

1 30 day rule

We note that the '30 day rule' in the Proposed Legislation, which applies to the decision period for consideration by the Treasurer of an application, remains the same as the '30 day rule' in the current legislation except that:

- an applicant may request that the Treasurer extend the decision period if FIRB has not completed its work in time or has asked for more time; and
- the decision period will be extended for the amount of time it takes for an applicant to provide any additional information requested by the Treasurer,[1]

(together, the **Additional Extensions**).

As noted in our Previous Submissions, we do not support the proposal to introduce a mechanism by which applicants voluntarily agree to extend the screening period. Nor do we agree with the proposal to allow FIRB to 'stop the clock' without any requirement of reasonableness.

The onus should not be placed on applicants to request an extension when FIRB has been unable to complete its analysis within 30days, regardless of the reason. Doing so gives applicants little choice but to concede to a request from FIRB that they request an extension, otherwise the applicant risks getting FIRB offside or having their application made public pursuant to an interim order.

If FIRB needs more time to consider an application, the onus should be on FIRB to seek a (confidential) order from the Treasurer that the time be extended. FIRB would need to justify its position. It should not be incumbent upon applicants to take actions to request an extension of time. In our experience, investors draw a lot of comfort from the fact that

[1] Paragraphs 82(5) and 82(6) of the Draft Bill.

the usual practice of FIRB is to deal with applications within 30 days. We are concerned that the new changes will effectively render the '30 day rule' meaningless, encouraging delay, creating uncertainty for investors and eroding investor confidence.

We understand that in large or complex matters, the option should be, and is, open to the Treasurer to make an interim order to extend the decision period, and this mechanism remains in place. However, diverging from the 30 day deadline should be the exception, not the rule and should be at the discretion of the Treasurer and not FIRB.

Recommendation: In our view, it would be preferable if the provisions for the Additional Extensions were removed and replaced with a mechanism that allows the Treasurer to grant an extension of the decision period, upon receiving an application from FIRB. The Treasurer should be able to grant an extension if he or she is satisfied that there are good reasons why a decision has not been made within 30 days.

2 Underwriter exemption

The inclusion of a clause providing for exemption certificates for underwriters is helpful;[2] however we consider the clause to be too narrow. The exemption applies only to 'financial services licensees authorised under the *Corporation Act 2001* (Cth) (**Corporations Act**) to underwrite securities' and does not extend to foreign government investors. In practice, entities outside this category are entitled to, and do, provide underwriting services[3] and we see no policy reason why they too cannot be entitled to apply for an exemption certificate.

In paragraph 3.7 of the Government's Options Paper entitled 'Australia's Foreign Investment Framework: Modernisation Options' (**Modernisation Options Paper**) released in May this year, the Government expressed its concerns about extending an exemption to un-licensed underwriters on the basis that such underwriting may not include a sell down obligation. We think this risk would be alleviated by the inclusion of a requirement that the exemption only apply so long as the underwritten securities are sold down to third party investors within 30 days and no voting rights are exercised by the underwriters in respect of the underwritten securities.[4]

In addition, the application process for an exemption certificate will allow the Treasurer to assess whether there is any risk to the national interest and to impose conditions if required.

Recommendation: We recommend:

- deleting paragraph 30(b) from section 30 of the Draft Regulations so that the section will apply to any foreign person (including foreign government investors) who propose to acquire an interest in securities in the course of their business of underwriting securities; and
- including a condition that the exemption will only apply so long as the underwritten securities are sold down to third party investors within 30 days and no voting rights are exercised by the underwriters in respect of the underwritten securities.

3 Dividend reinvestment plans

We support the importation of an exemption for dividend reinvestment plans into the Proposed Legislation from Australia's takeover rules, as proposed by the Government in their Modernisation Options Paper at paragraph 3.6. However, whilst an exemption has been included in the Proposed Legislation for pro rata rights issues, an equivalent exemption for dividend reinvestment plans has not.

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[2] Section 30 of the Draft Regulations.

[3] See section 611, item 13 of the Corporations Act for the exemption for underwriters under the takeover rules.

[4] This recommendation was made by the Law Council of Australia in their submission to the Government dated 19 June 2014, at page 8.

As noted in the Modernisation Options Paper, for most investors taking advantage of a pro rata rights issue or dividend reinvestment plan, 'their stake does not significantly increase, and they have no intention to seek control in their own right. With the announced introduction of fees, better targeting of applications is important to maintaining Australia's reputation as an attractive investment destination'.[5]

Recommendation: We recommend the inclusion of a dividend reinvestment exemption based on the definition of dividend reinvestment given in section 611, item 11 of the Corporations Act. Similarly to the rights issues exemption, this exemption should apply to foreign government investors.

4 12 month validity period

As noted in our Previous Submissions, we are concerned that (i) there is a default validity period for a no objection notification and that (ii) the default period is set at 12 months.[6] Given there are numerous situations in which FIRB approval is required for more than 12 months (e.g. exercise of share options and development of greenfields projects, which require property to be acquired over several years), there should not be a blanket validity period written into the Proposed Legislation.

Our concern is that as a matter of practice, when considering an application, FIRB officers will be reticent to allow a longer validity period as long as there is a statutory default period in place. In our experience, the 12 month period stated in the Policy is too readily relied upon, leaving investors with little flexibility to meet the needs of a transaction.

Recommendation: We would support a standard validity period (e.g. 3 years) set out in the Policy, but also the inclusion in the Policy of examples of circumstances in which the Treasurer would be prepared to give approvals which last for more than 3 years. Whether or not a shorter or longer period is granted should depend on the transaction in question and the national interest.

5 Australian non-resident citizens

We note that the definition of 'foreign person' in the Proposed Legislation continues to include Australian citizens who are not ordinarily resident in Australia despite the Modernisation Options Paper stating that the Government would consider refinements to the foreign person definition in relation to this issue.[7] As noted in our Previous Submissions, we see no policy reason for treating Australian citizens as foreign persons.

The definition of 'foreign person' in section 4 of the Draft Bill (which also applies under the *Register of Foreign Ownership of Agricultural Land Bill 2015* (**Register Bill**) can be compared to definitions in other legislation concerning foreign ownership of land, namely, Queensland's *Foreign Ownership of Land Register Act 1988* and Victoria's *State Taxation Acts Amendment Act 2015* which specifically exclude Australian citizens from the definition of foreign person:

- *Queensland's Foreign Ownership of Land Register Act 1988,* Schedule 1: 'foreign natural person means a person who is not an Australian citizen within the meaning of the Australian Citizenship Act 2007 (Cwlth) and..... '
- *Victoria's State Taxation Acts Amendment Act 2015*, section 14: 'foreign natural person means a natural person who is not any of the following - (a) an Australian citizen within the meaning of the Australian Citizenship Act 2007 of the Commonwealth...

Recommendation: We recommend expressly excluding from the definition of 'foreign person' in the Draft Bill a person who is 'an Australian citizen within the meaning of the

[5] Modernisation Options Paper, paragraph 3.6.

[6] Section 81(4) of the Draft Bill and section 50 of the Draft Regulations.

[7] Paragraph 3.9 of the Modernisation Options Paper.

Australian Citizenship Act 2007 (Cth)'. If that is not acceptable to the Government, we recommend at least the following:

- Extending the exemption in paragraph 25(b) (*Acquisitions by persons with a close connection to Australia*) of the Draft Regulations to subsidiaries of corporations or subsidiaries of trustees of trusts that are foreign persons only because of interests held in them by Australian citizens no ordinarily resident in Australia;
- Extending the exemptions in paragraphs 25(a) and 25(b) of the Draft Regulations to agribusinesses and other business acquisitions, or if this is not accepted, extending the higher threshold for:
  - 'agreement country investors' who invest in businesses or securities; and
  - 'relevant agreement country investors' who invest in agribusinesses,

  to Australian non-resident citizens and entities that are directly or indirectly owned by Australian non-resident citizens.

  Without such an exemption, US, Chilean and New Zealand nationals are afforded greater rights under the Proposed Legislation that Australian citizens, which seems curious given the aim is to regulate foreign investment.
- Finally, any exemptions included in the Proposed Legislation for Australian non-resident citizens should be mirrored in the *Register of Foreign Ownership of Agricultural Land Bill 2015* or the rules made pursuant to section 35 of that Bill.

If none of the above recommendations are accepted, we recommend at least amending section 5(1) of the Draft Bill (*Meaning of ordinarily resident*) so that it applies to any individual not just those who are 'not Australian citizens', as the current wording causes confusion as to whether an Australian citizen can be categorised as someone who is 'not ordinarily resident in Australia'.

6 Agreement country investor exemptions

'Agreement country investors' (as defined in the Proposed Legislation) theoretically receive the benefit of a higher $1,094 million threshold. Unfortunately, as noted in our Previous Submissions, the exemption has limited application given that it is not available to an agreement country investor who invests in Australian through an intermediate holding company or a special purpose vehicle which is incorporated in any jurisdiction other than an agreement country, even Australia (as is often the case). We see no policy reason for this limited application of the exemption.

Recommendation: We recommend amending the Draft Regulations so that the definition of 'agreement country investor' includes entities in which no less than 85.1% is held by entities constituted under the law of the jurisdiction of the relevant agreement country investor (i.e. the US, New Zealand, Korea, Japan or Chile), whether or not the first mentioned entity is incorporated or established in Australia or overseas, provided that the entity is not incorporated in a country that Australia does not maintain diplomatic relations with.

7 Exemption for acquisitions of land that is 'wholly incidental' to the investor's business activities

We note that the current legislation includes an exemption from the requirement to notify FIRB of the acquisition of an interest in Australian urban land if:

- 'the land is being used, or is able to be used immediately and in its present state, for industrial or non-residential commercial purposes; and
- the acquisition is wholly incidental to the conduct of the existing or proposed business activities of the foreign person (other than business activities that

include acquisitions of land or the development of, or investment in, land or the development or operation of any form of accommodation facility)'.[8]

This exemption has not been included in the Proposed Legislation despite the other regulation 3 exemptions for interests in Australian urban land being included in the Proposed Legislation and extended to apply to all Australian land. We consider such an exemption necessary to avoid immaterial acquisitions falling within the ambit of the Draft Bill. For example, a foreign government investor wishing to acquire a 5 year lease for a storeroom in an office building in order to store records would be required to seek the consent of the Treasurer notwithstanding that the acquisition is for little consideration and is wholly incidental to their business activities.

Recommendation: We see no policy reason why the existing regulation 3(f) exemption has not been migrated to the Proposed Legislation and we support its inclusion in the Draft Regulations. Similarly to other regulation 3 exemptions that have been included in the Proposed Legislation, the exemption should apply to foreign government investors.

8 Previous submissions

There are a number of concerns we have in relation to the Proposed Legislation which we have raised in our Previous Submissions, including those relating to:

- zero thresholds for foreign government investors;
- distinguishing between foreign governments on the one hand and sovereign wealth funds and state owned enterprises on the other;
- the imposition of fees; and
- regulation of internal restructures.

We do not repeat those concerns in this submission on the basis that we assume the Government has made a conscious policy decision on those matters.

We thank the Government for the opportunity to put forward our recommendations in this letter and look forward to discussing any of the matters contained herein if required.

Yours sincerely

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[8] Regulation 3(f) of the *Foreign Acquisitions and Takeovers Regulations 1989.*