31 August 2021

Manager Policy Framework Unit
Foreign Investment Division
The Treasury
Langton Crescent PARKES ACT 2600
FIRBstakeholders@treasury.gov.au

Dear Manager,

Thank you for the opportunity to respond to the consultation on the evaluation of the 2021 foreign investment reforms. This is an important issue for many Technology Council of Australia (TCA) members, and we welcome the chance to respond. We would be pleased to meet with the Treasury to discuss the points raised in our submission.

About the Tech Council of Australia and the Australian tech sector

The TCA is Australia's peak industry body for the tech sector. The Australian tech sector is a pillar of the Australian economy, contributing $167 billion per annum to the Australian economy, and employing 861,000 people. This makes the tech sector equivalent to Australia's third largest industry, behind mining and banking, and Australia's seventh largest employing sector.

The TCA represents a diverse cross-section of Australia's technology sector, from deep tech and software companies to VC firms and advisors. A number of our members operate or invest in businesses subject to foreign investment approvals, including multinationals and domestic firms, and venture capital funds.

Optimising for economic and security goals

Growing critical, strategic industries and technologies, such as AI, quantum computing, and space, is an essential objective of the Australian Government. The growth of these industries offers a double dividend for Australia. As high-value industries, they drive jobs, growth and exports. As strategic industries, they improve Australia's resilience and self-reliance, protecting Australia's national security.

These economic and security objectives can and must be mutually reinforcing. Growing critical industries that are dependent on government funding to survive leaves them financially fragile, and vulnerable to failure if government funding fluctuates. This is why Australia's Defence Industry strategy since 2016 has focussed on building sovereign defence capabilities that are economically resilient to peaks and troughs in official defence spending. It has done this by pursuing strategies such as encouraging firms to export, and to build a civil customer base alongside Australian defence industry contracts.

Conversely, where an industry or technology is of high strategic and economic value, it is increasingly important that the Australian Government has transparency on the strategic interests that control it, and how technologies are used and sold.

This latter rationale is the reason why Australia introduced the foreign investment reforms in 2020, which scrutinise foreign investment in strategic industries. Such scrutiny is common globally. Our member companies operating under the Australian scheme are subject to comparable frameworks in other jurisdictions.

The difference in Australia, however, is not the existence of the scheme, but its administration. In particular, the lack of timeframes for approvals for investment under the new national security provisions, and the lack of exceptions for low-value or low-risk activities. This means low-risk investments are subject to more uncertainty versus other jurisdictions, which makes Australia less attractive as an investment destination. This pressure applies to multinational companies (MNCs), who compare investment attractiveness across the different markets where they operate when choosing where to locate or expand activities. It also applies to domestic firms seeking to scale, and therefore attract global financing.

If this issue is not addressed, and it makes Australia less attractive for investment, then it can begin to impact the economic sustainability of firms and industries. This is because high-performing domestic firms lack the funding to grow, or are forced to relocate overseas to access it. For MNCs, it can means their operations in Australia find it harder to attract high-value activity, such as R&D hubs. Together, this stymies the growth of strategic industries, and lowers their resilience.

Improving the administration of the foreign investment review processes to reduce the impact on low-risk investments in strategic industries would therefore aid both Australia's economic and security objectives.

Implementation of the scheme

TCA members welcome Treasury's efforts to assist in easing the implementation burden of the scheme on industry by updating its website, providing guidance notes, and engaging with stakeholders. We also recognise that, as with the introduction of any new regime, it takes time to refine the approach.

However, our concern is that the guidance being provided by Treasury is not targeted at the elements of the scheme that are causing the greatest pain points for industry and investors. The areas where the industry needs clarity from the government are:

- Setting firm timeframes and deadlines for assessing investment decisions for simple and high-risk cases
- Whitelisting pre-approved and low-risk investors
- An improved approach to triaging referrals based on risk, e.g.:
    - A more streamlined approval process for pre-qualified investors that present a low risk (e.g. well-established VCs and investment banks from Five eyes countries)

- Setting thresholds under which investments must not be notified, e.g. where total investment is below a threshold, or where the company seeking investment is below a turnover threshold
- Setting triage criteria to assess the risk presented by an investment or company being invested in to help assign it to a simple or complex assessment, with corresponding and appropriate timeframes.

We would be pleased to work with FIRB and Treasury to identify if there are any other mechanisms for streamlining applications, such as exemption certificates.

Macroeconomic analysis

Invention and investment in strategic industries is a race. The first companies to create, patent and scale technologies, and the first investors to fund them, gain significant financial reward. This dynamic is particularly true in tech sector firms with either high capital costs to entry (e.g. quantum computing, space and defence) or network effects (many software and AI applications).

Australia is producing an increasing number of high-value ($100m+ valuation) tech sector firms. In the last five years, Australia has successfully grown a strong pipeline of 99 companies with valuations of $100 million or more.[1] Further, the number of companies being created in each of the last three decades is increasing rapidly, as Table 1 below shows. Being able to draw on foreign investment, such as through private investment and venture capital raises, is critical for firms that are scaling because Australia has a limited pool of capital to invest in scaling companies.

Table 1: Number of Australian tech sector companies

Decade of company formation	Current no. of companies founded in that decade presently valued at $100m+	Example companies
2000s	24	Domain, iSelect, Atlassian, Tyro, Health Engine, Finder, Red Bubble, Campaign Monitor, Envato, Hotels Combined, InfoTrack
2010s	67	Airwallex, Deputy, Brighte, 99designs, Airtasker, Koala, Stake, Prospa, Culture Amp, Compass, Sendle, Freelancer, Flare, Canva,

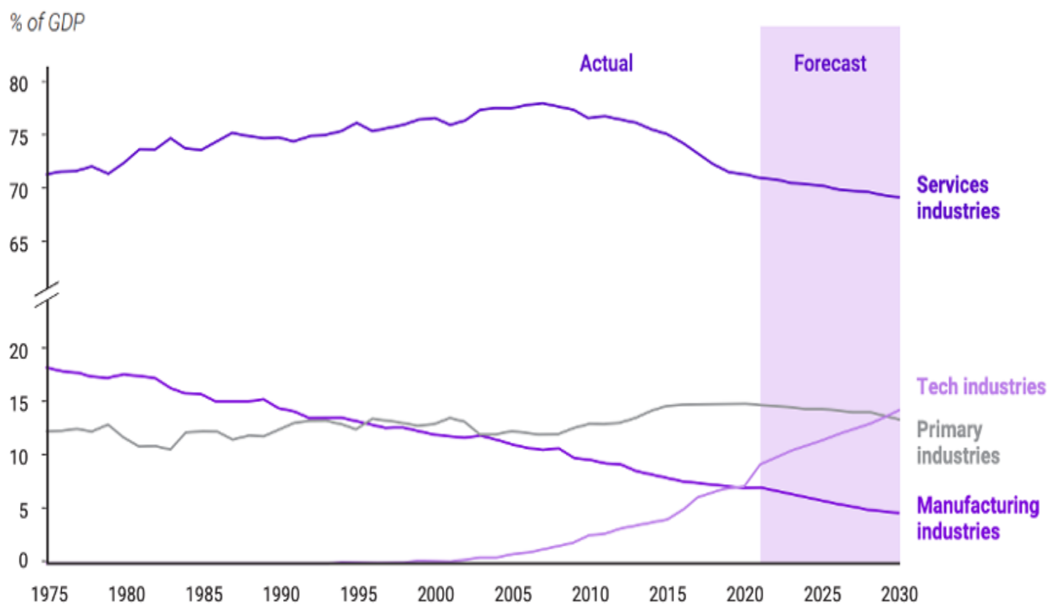
[1] Australian tech companies valued at $100M+ | by AirTree | AirTree | Aug, 2021 | Medium.com

		Expert360, Afterpay, Judo Bank, Shippit
Total	91	

Source: Airtree

This growth in Australian tech company creation and scaling means the tech sector is now a significant force in Australia's economy. Accenture forecasts that tech sector activity in Australia already exceeds manufacturing in its contribution to GDP, and is on track to exceed primary industries by 2030 (see Exhibit 1).

Exhibit 1: Contribution to GDP of Australian industry sectors, actual and forecast



Source: Accenture analysis of ABS 5204.0 Australian System of National Accounts, 2021

COVID-19 has vastly accelerated investment in tech firms in Australia and globally because it has increased demand for tech sector products and services. McKinsey has tracked the market valuations of 31 industry sectors globally since the COVID-19 pandemic began in February 2020. It finds that high-tech and advanced electronics are the second and third top industries for growth in valuation in that period. High-tech firm valuation increased from 8.4 trillion to 12.9 trillion, a growth of 55.82 percent in shareholder returns. Advanced electronics increased from 4.9 trillion to 7.7 trillion, a 56.2 percent increase in shareholder returns.

What that means in practice is that Australia should have witnessed a significant uplift in investment in private and public tech sector companies from February 2020 simply to keep pace with the rest of the world.

Australia's attractiveness as a site for investment

Australia must continue to be competitive at attracting the rapidly increasing amounts of investment available for the tech sector globally. Australia is a relatively small and remote market globally. That means domestic companies must work harder to attract customers, investors and set-up global exporting models. Local offices of MNCs also have to make a particularly compelling case internally for investment in the Australian market versus a more significant market such as the US, EU or Singapore.

Fortunately, the inventiveness and talent base of Australia in areas such as quantum computing and AI means that we can punch above our weight globally in invention and attracting investment. However, it is important Australia maximises the attractiveness of its regulatory settings and administrative processes to give local firms and MNCs offices located here the best chance to attract capital and investment.

Investors are not deterred by the presence of foreign investment screening in sensitive industries per se, because such regimes are now common in many countries, including the US, the EU, Japan and New Zealand.

However, the administration of Australia's foreign investment approval process is deterring investors because it is more uncertain and cumbersome compared with comparable processes in other jurisdictions. For example, it is common that if a firm in a strategic industry undertakes a raise, it receives investment from investors in multiple jurisdictions. This means firms go through multiple national approval processes simultaneously. Our member companies experience is that Australia is often the last jurisdiction to complete the assessment, even though we are one of the smallest markets and therefore have a lower volume of applications to process

The uncertainty of the Australian approach is now actively deterring foreign investors from investing in local firms, and participating in raises. For example, Q-Cntrl reports that three investors cited the new foreign investment review process as a reason not to invest in a recent raise. Investors are being disincentivised from investing in Australia because the current approach does not meet basic investor requirements, such as certainty that an investment will be reviewed in a specified time period. Fixing this simple issue by specifying timeframes and deadlines for approvals would make a material difference to incentivising investment in Australia.

Reform analysis – national security

The TCA supports the need for national security screening of investment in sensitive sectors to protect Australia's national interests. Most companies operating in sectors that fall into this definition export and are also subject to similar schemes in other jurisdictions. The need for such a framework in Australia, and its core concepts, are therefore well-understood.

Where there is considerable industry uncertainty is over the administration of the Australian scheme, and in particular, the timeframe for approving foreign investment applications. Currently, this can range from 1 – 7 months. That means anyone seeking foreign investment – including via low-risk channels such as a venture capital firm capital raising round – needs to plan for that raise on the basis of a potential 7 month wait. That timeframe is too long for VC firms to wait on during a capital raise. For example, Q-CNTRL reports that uncertainty over timing required them to undertake a raise earlier than anticipated, which resulted in a 30 - 50 percent valuation discount.

TCA members recommend Australia adopts the US Federal Government's model of automatically approving voluntarily notified investments within 45 days. This places an onus on the regulator to efficiently assess simple cases to avoid deterring investment or creating unnecessary uncertainty and cost for businesses.

Setting and meeting a 45 day timeframe should not present a challenge to FIRB. In stakeholder consultations, the Treasury has advised that the median time for assessment is now 49 days. If approvals are already routinely able to be made in this timeframe, setting 45 days as a clear deadline for lower risk applications would vastly improve investment certainty, without materially impacting resourcing.

Reform analysis – compliance, streamlining and fees

We have not observed that compliance measures associated with the scheme presents an issue for investors or firms per se, as both investors and firms respect the need for compliance with such schemes. Rather, the concern is that uncertainty over processing times deters investors from considering investments that would be required to go through the new process.

The TCA welcomes the streamlining measures introduced for less sensitive investments, particularly changes to the treatment of passive foreign government investment. We recommend a similar approach is taken to streamlining low-risk sensitive investments as discussed above.

The reality of fees charged in the screening process is that they are passed on to the Australian firms seeking investment, rather than absorbed by foreign investors. That means the scheme effectively imposes a cost on fast-growing Australian businesses seeking investment. Member firms can in general accept paying fees for approvals. What they really seek is minimum service standards for the service performed for the fee they are charged. This includes greater effort to streamline approvals for low-risk investors and investments, and also clear timeframes for low-risk approvals.

The exception is young, start-up firms which have limited funding and resourcing, and therefore are disproportionately impacted by fees. These will also be the firms that may find it harder to attract funding as they are younger and have less global profile. If the government is unable to introduce a threshold for investment under which investments need not be passed through the approval process, it could waive fees for firms whose turnover is below a threshold, at least reducing the cost burden on them.

TCA Recommendations

Improve the administration of the foreign investment review provisions for notifiable sensitive investments by:

- Introducing a 45 day approval deadline for non-complex approvals in sensitive industries
- Streamline approval processes for low-risk investments, e.g. through exemption certificates, whitelisting or by re-introducing a threshold below which an investment is not required to be approved
- Consider waiving fees for approvals where the company in which the investment occurs has a turnover below a certain threshold (e.g. $50 million to align with the Australian Taxation Office definition of a small business for the purposes of the small business tax cut).

****

We appreciate the opportunity to contribute feedback to the ideas proposed in this submission and look forward to ongoing dialogue.

Yours sincerely,

Kate Pounder
CEO, Tech Council of Australia
e: kate@techcouncil.com.au
m: +61 402 110 498