SQUIRE PATTON BOGGS

Proposed Reforms to Australia's Foreign Investment Review Policy

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On 5 June 2020, the Federal Treasurer announced major reforms to Australia's Foreign Investment Review Board (**FIRB**) rules. The government proposes to legislate these changes before the end of the year, with the changes to come into effect on 1 January 2021 and to replace the temporary changes to Australia's FIRB rules, which were implemented on 29 March 2020 in response to the coronavirus pandemic (**COVID-19**).

We have provided a summary of the proposed changes below. In short, the Treasurer will be prioritising national security in their assessment of proposals. The Treasurer will have powers to unwind a transaction after approval and where a transaction is not subject to the FIRB rules, and will have more powers to enforce compliance with FIRB approval conditions. More detail in relation to the proposed changes in full can be found in a Booklet, entitled '*Foreign investment reforms*', published by the Federal Treasurer.

New "National Security" Test

Under the proposed reforms, foreign investors seeking to acquire a "sensitive national security business" will have to pass a new national security test, which will assess proposals that give rise to national security concerns. The Australian Security Intelligence Organisation Act 1979 (Cth) defines security to mean protection from espionage, sabotage, politically motivated violence, attacks on Australia's defence system, acts of foreign interference or the protection of Australia's territorial and border integrity from serious threats. These factors may be relevant for the Treasurer when considering whether a proposed investment gives rise to national security concerns, but the criteria for this test is yet to be confirmed.

Retention of the "National Interest" Test

For clarity, the existing national interest test will remain unchanged. In order to avoid an overlap between the two tests, wherever the broader national interest test would apply to a particular action, only that test will be used in an assessment. This is because national security is already a relevant factor that the government considers as part of the national interest test.

Mandatory Pre-investment Notifications

Mandatory notifications are being introduced for two types of investment, which must occur prior to that investment. The mandatory notification will apply regardless of the value of the acquisition, where a foreign person acquires a direct interest (which is generally at least 10% or where the investor is in a position of control) in a sensitive national security business or where the business or entity owned by a foreign person starts to carry on a sensitive national security business.

Introduction of Sensitive National Security Business

Importantly, the definition of "sensitive national security business" will be narrower than that of "sensitive business" under the Foreign Acquisitions and Takeovers Act 1975 (Cth).

The term "sensitive business" refers to media, telecommunication, and transport businesses and businesses providing infrastructure to these businesses. Whilst, consultation has not begun on the new definition of "sensitive national security business" it is more likely to include:

- A businesses regulated under the telecommunications and critical infrastructure legislation in Australia
- Businesses involved in the manufacture or supply of defence or national security-related goods, services or technologies
- Businesses which can create vulnerabilities in the security of Australia's defence force or national security supply chain
- Any business or land situated in or proximate to defence or national security installations
- Any business that owns, stores, collects or maintains sensitive data relating to Australia's national security or defence

Most of the sectors that fall within the proposed definition are already considered sensitive under the existing legislation, which means they are already subject to a reduced monetary screening threshold, with the exception of the final point related to businesses that own, store, collect or maintain sensitive data. This reform is a timely and expected amendment that is very much aligned with international updates to foreign investment review policy. With this in mind, the reforms are unlikely to have a substantial impact on businesses operating in these sectors.

"Call in" Power

It is proposed that there will be a new "call in" power which permits the Treasurer to "call in" any investment before, during or after the investment, on a case-by-case basis if the Treasurer considers the investment is a national security concern. Once called in, an investment will be reviewed under the new "national security" test to determine if it raises national security concerns.

The proposed power will be time-limited and public guidance will be issued on the type of investment where the "call in" power could be used. If this power were introduced, it would be prudent that moving forward, transactions that do not require FIRB approval be conditional on the transaction not being "called in" during a set time frame.

"Last Resort" Review Power

It is proposed that there will be a "last resort" review power that allows the Treasurer to reassess approved foreign investments where subsequent national security risks emerge. The power permits the Treasurer to impose conditions, vary existing conditions, or, as a last resort, require the divestment of foreign interests in a business, entity or land. This power is necessary in order to keep the foreign investment framework at pace with emerging risks and global developments. For instance, where there is a rapid technological change and the conditions to protect national security have been made redundant or where the nature of the security risk changes subsequent to approval. Importantly, the last resort review power will not be retrospective, therefore proposals that have already been approved should not be affected.

Changes to the Classification of "Foreign Government Investors"

The proposed reforms will result in certain entities no longer being treated as foreign government investors, where no foreign government investor has management rights or influence or control over the investment or operational decisions of the entity. This will be given effect in two ways:

- Entities which have more than 40% foreign government ownership in aggregate but less than 20% from any single foreign government will no longer be deemed foreign government investors (where there is no influence or control)
- Entities which have a single foreign government with at least 20% ownership without influence or control will still be deemed foreign government investors, however, they will be able to apply for a broad exemption certificate on a case-by-case basis.

This reform is intended to make it easier for foreign investment funds with passive foreign government investors to invest in Australian assets and businesses. As under the present FIRB rules, foreign investment funds are required to "trace" foreign government interests through their ownership structures to identify government investors and to seek FIRB approval for a broad range of transactions regardless of whether these foreign government interests are passive or not.

Stronger Penalties, Compliance and Enforcement Powers

Finally, the federal government will have more powers and resources to enforce compliance with FIRB approval conditions and there will be stronger penalties for breaches. These powers may include, additional monitoring and investigative powers, powers to give directions to investors where there is a suspected breach of a condition, increased civil and criminal penalties, an expanded infringement notice regime and powers to remedy situations where incorrect statements or omissions are made on an application that result in a no objection or exemption certificate being issued.

The tougher compliance measures follow complaints that some foreign investors ignore the conditions that are attached to approved bids. This has come about as increasingly, conditions have been applied to allow bids to pass. In 2018-19 the number of approvals made subject to conditions increased to around 48 per cent of the total number and over 80 per cent of the total value of approvals.

Please do not hesitate to contact us if you have any queries. We note these proposed reforms have only just been released and we will endeavour to keep you updated of any additional updates.

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