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Australia's foreign investment (FIRB) regime reforms – where are we up to?

Four weeks out from the proposed commencement of the Australian Government's reform package for Australia's foreign investment regime and the detail still remains to be seen.

Since the 5 June 2020 Treasurer's announcement of major proposed changes to Australia's foreign investment laws (see our earlier insight), there has been a significant amount of draft legislation and explanatory material to work thorough. Following the release of exposure draft legislation and regulations in two tranches over July and September, the proposed amendments to the *Foreign Acquisitions and Takeovers Act 1975* (Cth) (the **Act**) were introduced into Parliament at the end of October. The legislation was then referred to the Economics Legislation Committee in the Senate, which recommended that the amendments be passed in its report dated 26 November 2020.

Despite all of this, if passed, the reforms are intended to commence on 1 January 2021 and are intended to coincide with the reinstatement of the pre-Covid monetary screening thresholds for foreign investment transactions that are subject to the Act (subject to indexation).

The reforms are the most significant since the introduction of the Act in 1975 and will shift the focus of the regime to Australia's national security. We are however yet to see the revised form of the proposed regulations, which means that the particulars of some of the key concepts being introduced by the amendments, are still unknown.

Key elements of the proposed reform focussed on Australia's national security include:

- A new national security test for foreign investors who will be required to seek approval to start or acquire a direct interest in a 'national security business' or to acquire an interest in 'national security land' – regardless of the value of the investment.
- A time-bound 'call in' power enabling the Treasurer to review acquisitions that would not ordinarily require notification where they raise national security risks.
- A national security last resort review power that will provide the Treasurer with the ability to reassess approved foreign investments where new national security risks emerge.

Other material changes will include:

- stronger monitoring and investigative powers, more flexible enforcement options and significantly higher civil and criminal penalties;
- measures to streamline investments by passive investors into non-sensitive sectors; and
- more involved and ongoing reporting obligations for foreign investors,

although we do not expand on these changes in this insight.

These reforms will add further complexity to what is an already complex regime and will significantly increase the level of scrutiny and compliance obligations that foreign investors will need to contend with.

Amendments to the fee regime for FIRB applications are also included in the reform package, which will see a significant increase in application fees for some types of investments.

The current position

Currently under the Act, if an action is taken by a foreign person, such as the acquisition of securities in an Australian entity, an acquisition of assets of an Australian business, or an acquisition of an interest in Australian land, it may constitute:

- a notifiable action;
- a significant action; or

The difference is:

- If an action is a notifiable action, the foreign person must notify the Treasurer and seek approval prior to taking the action. Failure to do so is an offence.
- If an action is a significant action, there is no positive obligation to notify the Treasurer of the action – however if the Treasurer becomes aware of the action, the Treasurer has the power to impose conditions on the action or to make orders stopping the action being taken, or unwinding the action (such as by making a disposal order), if the Treasurer is of the view that the action is contrary to Australia's national interest.

The proposed national security changes

Notifiable national security actions

Under the proposed reforms, a third category of action will be introduced to the Act – a 'notifiable national security action'.

A notifiable national security action involves a foreign person:

- acquiring an interest in certain types of Australian land (termed 'national security land');
- acquiring a direct interest in a 'national security business'; or
- starting a 'national security business'.

Foreign persons proposing to take a notifiable national security action must notify the Treasurer prior to taking the action, regardless of the size or value of the investment. This is intended to close the current loophole in the Act, which permits highly sensitive transactions to occur without scrutiny by the FIRB, simply because monetary thresholds are not met.

The proposed definition of a 'national security business' is extensive, and covers more than a page in the draft regulations. Broadly speaking, the intent behind the definition is to capture businesses involved in or connected with critical infrastructure, defence or the national intelligence community or their supply chains.

Significant concerns in relation to the breadth of the proposed definition and its clarity were raised during the consultation process on the draft reform package. In particular, concerns were raised around the proposed definition of 'national security business' being linked to terms in the *Security of Critical Infrastructure Act 2018* (**SOCI Act**), which is also currently the subject of proposed amendments. In addition to the critical electricity, gas, water and ports assets currently covered by the SOCI Act, those amendments propose to expand the scope of the SOCI Act significantly to cover sectors such as education, food and grocery, health, transport, banking and finance and data storage and processing.

Whilst the regulations incorporating this definition will only be released once the proposed amending legislation is passed, it is understood that this concept will remain. This means that the extent and impact of the proposed national security amendments may have much broader reach than originally anticipated.

The types of Australian land that will be the subject of a notifiable national security action are also yet to be settled, as this will be provided for in the regulations. However the draft reform package suggests that this will primarily capture defence premises and land in which an agency in the national intelligence community has an interest.

It is also important to note that a notifiable national security action (where it is *not* also a significant action) will be assessed against factors that give rise to national security concerns, rather than the broader national interest test that applies to significant actions and notifiable actions. We expect further guidance will be released by the FIRB closer to the implementation date as to exactly how this will be interpreted.

Call-in power

The Treasurer will be afforded with new powers to "call-in" certain actions by foreign persons for review, even where those

actions were not significant actions or notifiable actions, where the Treasurer is of the view that an action may pose a national security concern.

It is proposed that the Treasurer will be able to review:

- any significant action that was not voluntarily notified to the Treasurer; and
- any 'reviewable national security action'.

A 'reviewable national security action' is broadly defined and may include:

- acquisitions of any interests in an entity or Australian business;
- acquisitions of interests in Australian land;
- issuing securities in an entity;
- entering or terminating a significant agreement with an Australian business;
- entering agreements relating to the affairs of Australian entities;
- altering the constituent document of an entity; and
- starting an Australian business.

The aim is to capture those actions expected to give foreign persons potential influence and rights, such as the ability to influence or participate in the central management or policy of an entity or business, or the right to occupy Australian land.

Acquisitions of interests in entities and businesses that do not amount to a direct interest – for example, interests of less than 10 per cent in an entity – are not reviewable national security actions unless the foreign person will also be able to participate in the central management and control of the entity or will afforded rights to influence or participate in the policy of the entity.

If a review notice is issued in relation to a particular action, the Treasurer's powers in relation to the reviewable national security action will be similar to the powers in relation to significant actions, in that the Treasurer may:

- impose conditions on the action;
- prohibit the action, if it has not yet been taken; or
- if possible, unwind the action, by making disposal orders.

The draft regulations proposed that the Treasurer will have a period of 10 years from the relevant action being taken to exercise the 'call-in' power. This time period was also the subject of significant concerns raised throughout the consultation process on the draft reform package and it remains to be seen whether the Government will reduce this time period in the final regulations.

Notably, a foreign person will have the ability to voluntarily notify of a transaction to eliminate the risk of later being called-in. Similarly, exemption certificates that cover a proposed action will also protect against a call-in risk.

Last resort power

Currently, after the Treasurer has been notified of a significant action or a notifiable action, and has provided a no objection notification in relation to that action, the Treasurer may not amend the no objection notification (or any attached conditions), if to do so would be detrimental to the foreign person (unless the foreign person consents).

The new last resort power will give the Treasurer the power to review an action that was the subject of a no objection notification at any time if:

- there has been a material misstatement or omission in the information provided to the Treasurer in connection with the person's FIRB application process that directly relates to a national security risk;
- the business, structure or organisation of the person has, or the person's activities have, materially changed and that change could not have reasonably been foreseen or was remote; or
- the circumstances or the market relevant to the action have materially changed and have altered the nature of any national security risk.

In reviewing the action, the Treasurer will be required to consider whether a national security risk exists in relation to the action. In doing so, the Treasurer must have regard to advice provided by agencies in the national intelligence community. The person who is the subject of the review needs to be notified of the Treasurer's review, unless doing so would prejudice Australia's national security interests.

If after reviewing an action, the Treasurer considers that a national security risk exists, the Treasurer will be required to give the person notice of this risk and of the reasons for this opinion (which may be redacted on grounds of national

security).

The foreign person is able to apply to the Administrative Appeals Tribunal for review of the Treasurer's decision that a national security risk exists.

Depending on the outcome of the review, the Treasurer will be able to make orders:

- prohibiting a proposed action;
- ordering the disposal of any asset or interest acquired; or
- varying the conditions of the no objection certificate, or imposing new conditions.

Before making an order, the Treasurer will also be required to (among other things):

- take reasonable steps to negotiate in good faith to eliminate or reduce the national security risk to avoid giving the order; and
- be satisfied that the use of all other regulatory systems of the Commonwealth, States and Territories would not adequately eliminate or reduce the national security risk.

Timing of actions

Importantly, the above national security amendments will not have retrospective effect and will only apply in respect of actions that are taken or proposed to be taken on or after 1 January 2021.

Takeaways

The suite of national security reforms discussed above will significantly change the regulatory environment for foreign investment in a range of sectors and will undoubtedly add to the complexity of the regime.

There will be matters in the amended legislation that will need to be the subject of additional FIRB guidance notes so that foreign investors (and their advisers) can understand Treasury's position on the interpretation and application of the new laws and we suspect that this will be an evolving set of guidance notes that are expanded as and when we start applying the new regime.

With significant increases to penalties for non-compliance also set to be introduced from 1 January 2020, it will be more important than ever for foreign investors to understand the nature of the changes and how they will be impacted.