

BCA

Business Council of Australia

# Consultation process on 2022 Foreign Investment Reforms

Submission

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# 1. About this submission

The Business Council of Australia (BCA) welcomes the opportunity to provide the Government with comments on options to enhance Australia's foreign investment framework. Within the short time in which submissions were open the BCA has consulted a range of business leaders across the legal, energy, retail, manufacturing, information technology, property, financial services, and banking sectors. There continues to be a high level of concern about the operation of the foreign investment screening process.

## 2. Key recommendations

The BCA acknowledges the important role of FIRB and the Treasury in administering foreign investment screening in Australia and the challenges involved in balancing the benefits of foreign investment with legitimate national security considerations.

Within the last year, we have undertaken extensive consultation with members and developed a set of practical recommendations on how the foreign investment framework can be improved, which remain current.

The BCA recommends improvements to Australia's foreign investment screening regime through:

1. Faster processing times and greater accountability by establishing a 21-day maximum deadline on FIRB's consult agencies;
2. Providing additional training opportunities for FIRB officers and relevant consult agency officers to ensure better understanding of commercial processes;
3. Improved targeting of material risks by moving non-sensitive, routine transactions to a register system;
4. Relieving pressure on the volume of cases by introducing a client-focused Trusted Investor scheme;
5. Enhancing flexibility of exemption certificates and clarifying language used when outlining conditions;
6. Making compliance easier by reducing complexity and introducing more standardised conditions, rather than focussing on enforcement through increasing sanctions for non-compliance; and
7. Benchmarking Australia's screening system to international best practice to ensure we are not at a competitive disadvantage.

## 3. Overview

### 3.1 The importance of foreign investment

Foreign investment is as critical as ever to the Australian economy. To secure Australia's recovery from COVID-19 it is essential that Australia turns around its business investment performance and central to that will be creating the conditions to attract greater levels of foreign investment and for Australian companies to have the confidence to invest in major projects.

Problems with the FIRB process are not only sending a negative message to foreign investors but putting sand in the wheels of Australian companies seeking to invest in the domestic economy.

There has been a major reduction in investment flows over the past two years, and there remains today a net outflow of investment from Australia (see data below).

We cannot afford to be complacent and assume Australia's attractiveness as an investment destination will continue and that current policy settings will see foreign investment return to pre-pandemic levels. We must move away from a Fortress Australia mentality and send a clear signal that Australia is truly open for business by

removing barriers. This includes reducing the heavy regulatory burden that companies face in looking to invest in Australia.

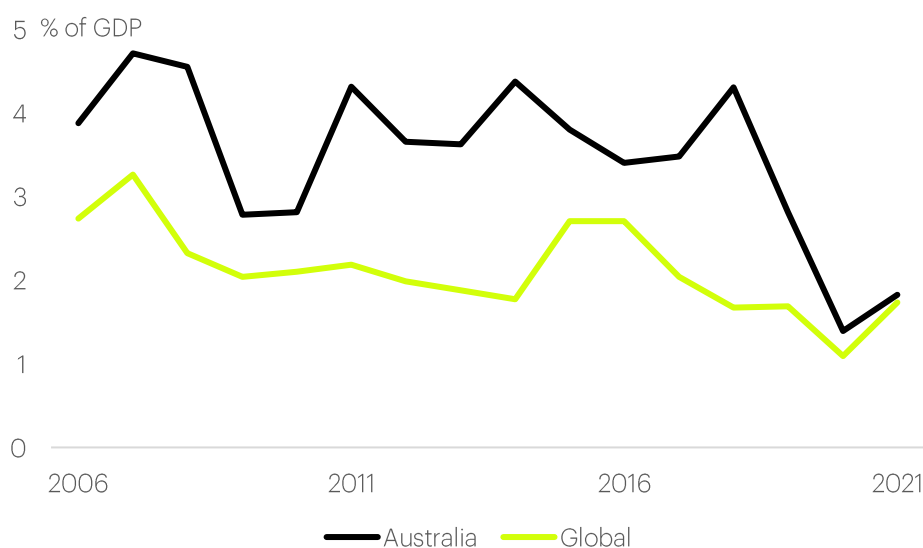
Poorly designed foreign investment screening can dampen investment, impacting on job creation and wages growth. It must be acknowledged that the pervasive nature of Australia's foreign investment regime and process issues are making routine and non-sensitive business transactions unnecessarily complex and time-consuming, sending a concerning signal to the investors we depend upon to grow future prosperity.

### 3.2 Foreign investment into Australia has not recovered

Australia has been a net capital importer for most of the past 200 years. That is, foreign investors have tended to invest more in Australia than Australians have invested offshore. However, in 2019-20 there was a net outflow of capital for the first time since the 1970s. There was another net outflow in 2020-21, with the two consecutive years of outflows a first since the late 1940s. This reflects a mix of both falling investment into Australia and increased investment offshore, including by superannuation funds.

There are many factors that influence foreign direct investment (FDI) inflows into Australia. From a macroeconomic perspective, Australia's economy has outperformed that of many other advanced economies the past two years. Indeed, this is reflected in FDI data with FDI inflows bouncing back in 2021. However, while FDI inflows have recovered globally, they remain well below pre-COVID levels in Australia.

Figure 1: FDI inflows as a share of GDP



Source: ABS, UNCTAD and IMF

Treasury has suggested that strength in FIRB applications can be taken as a sign that Australia remains an attractive place to invest. But as pointed out in the 2016 Treasury Working Paper on foreign investment 'The FIRB statistics do not measure total foreign investment made in any year, nor do they measure changes in net foreign ownership levels in Australia. The data collected by the FIRB is based on approvals for proposed rather than actual direct investments above certain notification thresholds that differ by country and type of investor'.

Recent strength in applications will also have been influenced by increased M&A activity in the wake of disruption from COVID. These investments do not equate to new fixed capital formation and should not be mistaken as a sign of Australia's attractiveness as an investment destination.

## 4. Substantive comments in response to discussion paper

In the past two years, FIRB's powers and its regulatory reach has significantly expanded, first through a temporary lowering of monetary thresholds due to the pandemic, and then through major national security-related legislative reforms.

These changes have been important to support public confidence in the investment screening system, particularly to keep pace with emerging technologies and the changing strategic environment. However, while FIRB is empowered to identify and address these risks, much more can be done to address regulatory frictions and modernise a system that dates back to the 1970s.

The Chair of FIRB, David Irvine AO, has stated that the role of FIRB is to facilitate rather than impede foreign investment in Australia<sup>1</sup>. This needs to be the guiding principle when considering how to improve the current system.

### 4.1 Reducing the regulatory burden

Greater legal and regulatory certainty combined with a professional, client-focused approach would go a long way towards attracting and securing investment into Australia. This is as much about supporting Australian-owned and Australian-managed firms to do business, to partner internationally and change and adapt with the global economy.

#### Improve processing times

In our consultation with members, processing times for applications are commonly cited as the most pressing problem businesses face when dealing with the FIRB system. Despite the 30-day statutory target, anecdotal evidence suggests larger business transactions continue to be unduly delayed, with reports of 6 to 12 months far from uncommon.

Such delays can have a material impact because major investments typically involve M&A project teams and large project implementation teams. These are established and funded in advance of application and continue to operate during the decision period to ensure implementation can occur upon approval. The cost of delays can often be in the millions.

One of the most common reasons provided by FIRB for delays is that advice is pending communication from a consult agency. These agencies include the ACCC, the ATO, the Department of Defence, the Critical Infrastructure Centre, ASIO and several others depending on the nature of the application. While FIRB is accountable for the timeliness, professionalism and commercial acumen of its own staff (and feedback suggests this is largely positive), the consulted agencies are one step removed from the process and, as a result, only indirectly accountable to the client's needs.

FIRB clients report opaque decision making and irrelevant enquiries from consulted agencies. Often questions are asked that have little to do with the type of business or transaction being undertaken. At times questions relating to matters like competition and taxation can appear to be opportunistic regulatory fishing expeditions.

- **Recommendation 1:** To resolve the delays in application approvals related to the agency referral and consultation process, administrative time limits should be imposed on consulted agencies. This would provide that:
  - Referred agencies provide advice within 21 days of the application being referred, or consent is presumed

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<sup>1</sup> Source: <https://firb.gov.au/about-firb/news/address-david-irvine-ao-chair-foreign-investment-review-board-international-ceo>

- Where the advice of two or more agencies conflicts, resulting in processing delays, the Treasurer is empowered to step in and make a determination.

### Improve customer service focus

Members noted with regret that they are not getting reliably good service for the very high fees charged. Feedback suggests that FIRB officers are generally perceived as being professional, however there is a common sentiment among businesses that regularly deal with FIRB that it is “pot luck” whether they are assigned a FIRB officer who is experienced and knowledgeable about business processes and will process their application expeditiously.

High staff turn-over means clients face a carousel of different case-officers, with new officers often requiring information about an entity or transaction which has already been communicated in prior exchanges. There are also unfortunate anecdotes where FIRB officers have delayed processing transactions by not applying common sense and asking additional questions that should be self-evident.

While Treasury has been increasing capabilities in terms of resources and commercial stakeholder training for FIRB staff, judging by the way commercial deadlines are treated and the types of conditions that are being applied, the commercial and regulatory capabilities in consulted agencies has considerable room for improvement. Addressing the accountability, stakeholder responsiveness and commercial exposure of consulted agencies should be a top priority for the investment screening system as a whole.

Given the high fees charged, which are in themselves a potential deterrent to investment, a greater focus on customer service is required. Investors coming to Australia provide much needed capital, technology and know-how that boosts employment and growth, and should be treated as such.

- **Recommendation 2:** The Business Council would be happy to assist in providing training opportunities to FIRB officers and relevant consult agency staff on commercial processes. Business could look to provide such training directly and in person, which could have the benefit of increasing mutual understanding and fostering improved client-focused relationships, rather than transactional ones.

### Streamline non-sensitive, routine transactions

There are significant opportunities for further streamlining of FIRB’s operations so that it is targeting the types of foreign investments Australia ought to be avoiding, while ensuring more appropriate investments aren’t unduly delayed. The expansion of the Treasurer’s powers to enable him or her to take actions after an investment has been made significantly diminishes the case for needing to screen all transactions up front.

Changing the notification requirements for non-sensitive, routine transactions so they do not require a screening process to proceed, but only require the registration of information so FIRB has adequate knowledge of the transaction, would make a significant difference in the case load. Such transactions could apply to:

- commercial property leases
- small land acquisitions that are incidental to land already approved
- buy-backs
- Australian entities that have no Australian assets
- corporate re-organisations in which there is no change in ultimate beneficial ownership
- bolt on transactions, and
- existing shareholders making creep investments within certain parameters.

Members have raised examples where transactions are being caught by the FIRB system on a technicality, including where the entities involved in a transaction are all Australian.

Under the recent reforms, the Treasurer has acquired new call-in and last resort powers. Given these safeguards now exist, there are ample opportunities for risks identified following the completion of a transaction to be

addressed after the fact. This should provide greater confidence for FIRB to take a softer approach at the front door and move to a register system.

- **Recommendation 3:** Implement a new system for registering non-sensitive transactions. The new consolidated Register of Foreign Owned Assets, for which the Government has already committed \$86.3 million over four years, should be developed as a risk triaging tool for this purpose.

#### Reduce volume of cases by introducing a client-focused Trusted Investor scheme

Where FIRB's regular clients can demonstrate a track record of appropriate and prudent decision making, a Trusted Investor profile could be established in which client ownership structures and equity changes are recorded and updated as required. This would allow a 'tell-us-once' regulatory approach to the specific transactions undertaken, reducing the time cost for both investors and FIRB.

- **Recommendation 4:** Utilise existing best practice regulatory models, such as Australian Border Force's Australian Trusted Trader scheme, to develop a Trusted Investor scheme.

## 4.2 Exemption certificates

Although the exemption certificate system has been promoted as a streamlining mechanism that allows a client to undertake a series of investments, they have not performed this role in practice. While their intent is to reduce the regulatory burden, from our consultations, there was a sense that exemption certificates are too complex and have lost flexibility, rendering them impractical for the end user.

Several users of the system report that the process of obtaining exemption certificates can be extremely prolonged – up to 12 months in some cases. In such cases the value of certificates to execute time sensitive transactions is completely lost. Reporting requirements under exemption certificates have gone from being annual to monthly, creating an additional heavy regulatory burden.

- **Recommendation 5:** In order to improve the exemption certificate system, consideration should be given to providing greater flexibility on time limits and financial caps and broadening of the private equity exemption.

## 4.3 Compliance and enforcement

The recent reforms to FIRB have put a much greater emphasis on conditions, the potential for comebacks and forced divestments, compliance monitoring and significant penalties for breaches. Once through the front gate, investors are not home free. FIRB now has an enhanced role policing risks, including future risks, behind the border. The various conditions applied over time form a patchwork of ad hoc and often commercially unworkable rules that foreign investors, and the Australian companies connected to them, are forced to comply with.

The increasing reliance on conditions for FIRB approvals has resulted in a variety of impractical conditions being imposed, which send mixed, and at times conflicting, signals to investors. Evidence suggests that the conditions attached to approvals are drafted with little regard for commercial realities, compliance, enforceability, and consistency with Commonwealth and State and Territory laws.

Our most recent discussions with members have revealed considerable concerns around the approach to conditions employed by FIRB. These are outlined below.

- There is a common sentiment that the reporting notifications under sections 98C, 98D, 98E are unclear and hard to understand, even for legal specialists. Given the penalties that can potentially follow from non-compliance, providing greater clarity regarding where the law applies is a high priority for action.
- There is an impression that the default attitude of FIRB is towards imposing more conditions, even when there are no clear national security grounds for doing so, rather than seeking to minimise conditions in order to facilitate regular business activity in the national interest.

- The lead time for identifying required conditions and obtaining clearance can be a significant impediment to foreign participation in transactions. Foreign investors can be put in an awkward position of negotiating with FIRB's legal unit while a deadline for a major deal is passing, causing uncertainty, delays and threatening successful participation in competitive processes. Given the delays in processing applications mentioned in section 4.1, some companies are accepting inappropriate conditions in order to proceed through the FIRB process, rather than seeking to negotiate more appropriate conditions and facing further delays. This clearly unintended outcome highlights the vital importance of improving application processing times.
- Fines and other penalties available for breaches are excessive and disproportionate. Given the complexities of complying with conditions, investors face substantial risks of potentially damaging penalties for non-compliance, even if these occur despite acting in good faith. There is a real possibility that given the risks involved, some investors will simply look at Australia and say it is 'too hard'.

### Make it easier to comply

Given the complexities in processes and the risks involved in non-compliance, one member expressed concern that some companies may need to hire a dedicated FIRB compliance officer, a situation which would clearly not be consistent with a client focussed system that is designed to facilitate investment.

In the context of the issues noted above, one member observed that the focus on compliance and enforcement suggested by the discussion paper was misguided and should be flipped around. In other words, if conditions were standardised to a greater degree and made easier to understand, this would go a long way towards ensuring compliance.

- **Recommendation 6:** To enhance compliance with the foreign investment framework, the focus should be on making it easier to comply by reducing complexity and introducing more standardised conditions, rather than looking at ways to increase sanctions for non-compliance.

## **4.4 Improve overall operation of foreign investment framework through benchmarking**

Australia is not alone, and indeed is often cited in the international community, for elevating and pioneering national security regulation in foreign investment and other economic activity. But when considering the whole-of-system transformation of FIRB, Australia is somewhat of an international outlier in terms of the level of scrutiny that foreign investment attracts.

- **Recommendation 7:** In order to ensure investment screening regulation is not putting us at a competitive disadvantage, we need to benchmark Australia's foreign investment system against peer mature systems.

It is also important that investment screening policy not be subjugated and ignored or treated as off-limits in global trade and economic policy. Australia has a track record of successfully reconciling legitimate non-economic objectives with open borders. We can play a role rehabilitating foreign investment policy as a priority in the OECD and stimulating engagement on governance and rules in the WTO and other trade negotiating fora. The development of measures need not interfere with sovereign national security policy, but they can address issues around minimum standards on transparency, due process and procedure in investment screening. Such a commitment would send a strong signal that Australia is open for business.



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