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Mr J. Hawkins
Secretary
Senate Standing Committee on Economics
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Mr Hawkins

INQUIRY INTO FOREIGN ACQUISITIONS AMENDMENT (AGRICULTURAL LAND) BILL 2010

I refer to your letter of 15 February 2011 to Mr Patrick Colmer concerning an invitation to make a submission to the above inquiry. I am pleased to provide the attached submission on behalf of the Department of the Treasury.

Please note that Mr Colmer has taken up a senior position elsewhere in the Department and his substantive replacement as General Manager of the Foreign Investment and Trade Policy Division is Ms Deidre Gerathy.

Yours sincerely

Frank Di Giorgio
Acting General Manager
Foreign Investment and Trade Policy Division



Australian Government

Department of the Treasury

Submission to

The Senate Economics Legislation Committee

Inquiry into Foreign Acquisitions Amendment (Agricultural land) Bill 2010

1 Introduction

The Australian Government Department of the Treasury (**the Treasury**) welcomes the opportunity to provide a submission to the Senate Economics Legislation Committee Inquiry into the Foreign Acquisitions Amendment (Agricultural land) Bill 2010 (**the Bill**).

This submission contains background information about Australia's foreign investment policy framework, including the administrative and legislative aspects of the framework. The Submission makes a number of observations in relation to the Bill which may be useful background for the Committee's examination.

2 Key Findings

The Submission concludes that aspects of the Bill warrant careful consideration by the Committee. The key points are:

- there is a lack of data to gauge the level of foreign ownership of rural land and water entitlements and whether that level is detrimental to the wellbeing of Australians. The Australian Government has asked the Australian Bureau of Statistics to collect data on ownership in the agricultural sector and the Rural Industries Research and Development Corporation to commission work on the role of foreign investment in the development of the sector, including the extent of foreign ownership of agricultural businesses.
- the Bill proposes regulatory changes that could be better informed about what problems need addressing;
- the Bill's economic and administrative impact has not been adequately addressed; and
- the regulations proposed in the Bill may be in breach of Australia's international obligations.

The proposed introduction of a 5 hectare threshold specific to agricultural land imposes significant burden on investors, both in absolute regulatory terms as well as in comparison with other regulatory notification and approval arrangements in the *Foreign Acquisitions and Takeovers Act 1975* (**the FATA**). The legislation of specific national interest criteria, as proposed in the Bill, will reduce flexibility in the Government's screening of foreign investment proposals, without adding to protection of the national interest (these factors have been typically used in practice), nor to transparency. There is a real risk that the changes could discourage foreign investment in this sector of the economy, which has made an important contribution to the growth and development of Australia's agricultural sector.

The Submission considers that the Bill does not present a sufficiently strong case to justify the regulatory changes it is suggesting. It also raises significant concerns about the potential economic, administrative and legal impact of a number of the specific measures included in the Bill.

3 Role of the Department of the Treasury

The Treasury's mission is to improve the wellbeing of the Australian people by providing sound and timely advice to the government, based on objective and thorough analysis of options, and by assisting Treasury ministers in the administration of their responsibilities and the implementation of government decisions. In carrying out its mission, the Treasury (and,

organisationally, Markets Group) has responsibility for policy advice ensuring the well functioning of markets. Well functioning markets contribute to improving national productivity and promoting stronger economic growth, which enhances the living standards of all Australians. The Foreign Investment and Trade Policy Division (**FITPD**) of Markets Group administers and, in consultation with the Foreign Investment Review Board (**FIRB**) and other relevant Australian Government Departments, provides advice on incoming foreign investment consistent with Australia's national interest. FITPD is also responsible for providing advice to the Australian Government on Australia's foreign investment policy framework.

FIRB is a non-statutory body responsible for advising the Treasurer and the Government on foreign investment policy and administration. FITPD provides secretariat services to the FIRB and is responsible for the day-to-day administration of the screening arrangements.

4 Background

Foreign investment has been important to Australia's agricultural sector for many years. According to anecdotal evidence, this investment has brought benefits to the sector and to the economy more generally. In addition to supplementing capital for development and expansion, foreign investment has helped to stimulate jobs on farms and support services such as harvesting, transport, and processing. Regional towns and communities have received flow-on benefits through local purchases of inputs, machinery, and the general necessities of life. New investment can help Australian agriculture to be more efficient, competitive and profitable in world markets.

From the perspective of foreign investors, Australia's agricultural sector has been an attractive place to invest. This attractiveness stems from Australia's reputation as a high quality producer; its proximity to key Asian markets; the counter seasonal production benefits it offers markets in the northern hemisphere; its low sovereign risk; and its enviable productivity record. It is not surprising that Australia continues to attract foreign investment as a top surplus food and fibre producer.

5 Regulatory context

Australia's foreign investment policy provides for Australian Government scrutiny of proposed foreign purchases of Australian businesses and real estate. Foreign investment proposals are subject to examination on a case-by-case basis under the FATA and Australia's foreign investment policy (**the Policy**). This examination enables the Government to consider whether a particular investment raises any national interest concerns. Proposals that raise national interest concerns can be blocked by the Government, or have conditions imposed to ameliorate such concerns.

The types of foreign investment proposals which are subject to the FATA or the Policy, and hence should be notified to the Government include:

- Acquisitions by private investors of an interest of 15 per cent or more of an Australian business or corporation that is valued above \$231 million (indexed annually). This includes acquisitions of offshore companies whose Australian subsidiaries or gross assets are valued above \$231 million.

- United States investment in non-sensitive sectors is subject to a higher threshold of \$1005 million (indexed annually) under the terms of the Australia-United States Free Trade Agreement.¹
- Investments in the media sector of 5 per cent or more regardless of size.
- Direct investments by foreign governments and their related entities regardless of the value of the investment.
- Acquisitions of interests in Australian urban land (including interests that arise via leases, financing and profit sharing arrangements) that involve:²
 - Developed commercial real estate, where the property is subject to heritage listing, valued at \$5 million or more;
 - Developed commercial real estate, where the property is not subject to heritage listing, valued at \$50 million or more;
 - Vacant land, residential real estate and shares or units in Australian urban land corporations or trusts – regardless of value;
- Proposals where the proponents have any doubts as to whether they must be notified.

Further information can be found in the Policy, which is available online at www.firb.gov.au. There are sector-specific laws and policies in particular industry sectors which are regarded as sensitive, such as in banking, civil aviation, airports, shipping, media and telecommunications.

5.1 Regulatory context - agriculture sector

Investment in the agricultural sector can take the form of the purchase of Australian agricultural land (AAL) or an agricultural business. The FATA uses the concept of “rural land” which is defined as land situated in Australia that is used wholly and exclusively for carrying on a business of primary production.³ If land cannot be considered AAL then it is defined as Australian urban land (AUL) and the acquisition would need to be examined under the FATA (as outlined above).

To be a business of primary production, the business must be substantial and have a commercial purpose or character. The definition of a primary production business is taken from the *Income Tax Assessment Act 1997*. It refers to production resulting from the cultivation of land; animal husbandry/farming; horticulture; fishing; forestry; viticulture or dairy farming. Primary production for the purpose of the rural land definition does not include vacant land (even if zoned ‘rural’), hobby farms, ‘rural residential’ blocks or land used for stock agistment or mining.

¹ On 16 February 2011 the Prime Minister signed an Investment Protocol with New Zealand to the ANZCERTA which, once implemented, will extend the US threshold to New Zealand investors.

² There are separate arrangements applying to developed commercial real estate in respect of US investors under the AUSFTA.

³ The definition, contained in Section 5 *Interpretation* of the FATA refers to “Australian rural land”. This labelling has been changed to Australian agricultural land (AAL) within this submission to align with labelling used in the Bill.

Whether a party's activities amount to the carrying on of a substantial business of primary production is assessed on a case-by-case basis. The nature of the activity, the party's intention and the method of operation help determine whether a business of primary production is being carried on. For further examples of businesses that do/do not fall into the primary production category see the Australian Taxation Office's ruling on "Am I carrying on a business of primary production?"

Investments by privately-owned foreign investors are subject to the general thresholds. As such, an acquisition of a business of primary production valued at \$231 million or more (\$1,005 million in the case of United States investors) requires prior approval.

Direct investments in AAL or agricultural businesses by foreign governments and their related entities need to be notified to the Australian Government for review, regardless of the size of the investment.

6 Foreign Acquisitions Amendment (Agricultural land) Bill 2010

6.1 Summary

In broad terms the Bill proposes to:

1. require the Treasurer to approve acquisitions of interests in AAL greater than 5 hectares in area (s 21B)
2. require the Treasurer to consult a checklist of "national interest" issues to be incorporated in the FATA before approving such an acquisition (s 21C); and
3. require the Treasurer to publish details of all AAL applications (s 21D).

6.1.1 Acquisitions of interests in AAL

Current situation: Acquisitions of interest in AAL by private foreign investors are generally exempt from foreign investment review, except where they occur through the acquisition of an interest in a company or business that owns rural land. In such cases, approval is required for acquisitions of 15 per cent or more of companies or businesses valued at \$231 million or more.

Proposed treatment: The Bill adds to this monetary threshold an additional agricultural land area threshold wherein all interests in agricultural land, as defined, of more than 5 hectares must be notified.

AAL is defined in the Bill as 'land used predominantly for carrying on a business of primary production'. An interest in AAL is taken to encompass:

- a legal or equitable interest in agricultural land;
- management rights;
- leases of more than 5 years; and
- profit-sharing arrangements (s 12D).

The Bill also applies to acquisitions of shares in a company or units in a trust in which AAL accounts for more than 50 per cent of its assets (s 13E and s 13F).

An acquisition of AAL could be blocked (s 21B(2) or unwound (s 21B(4)) if it is considered by the Treasurer to be contrary to the national interest. Criminal penalties apply for a failure to notify certain acquisitions (s 26B).

6.1.2 Legislated national interest test

Current situation: At present, there is no definition of “national interest” in the FATA. This has been the case under successive governments going back to when foreign investment was first regulated. The revised Policy, released in June 2010, provided a detailed discussion, for the first time, of factors that the Government typically considers when assessing foreign investment proposals: national security, competition, other Australian Government policies, including taxes, impact on the economy and the community and character of the investor.

Proposed treatment: The Bill prescribes a list of factors to which the Treasurer must have regard in assessing the national interest, namely:

- national security;
- competition;
- Australian tax revenues;
- the impact on the Australian economy or the community (which is defined extensively); and
- the character of the investor (s 21C).

6.1.3 Publication of agricultural land applications

Current treatment: Foreign investment applications are currently handled on a commercial-in-confidence basis. Some detail of a particular case may be available under a Freedom of Information (FOI) request, provided that availability to a FOI applicant does not contravene privacy law or business commerciality.

Proposed Treatment: The Bill would require details of all AAL applications to be published on Treasury’s website and updated weekly with details of the progress of each application (s 21D).

7 POLICY CONSIDERATIONS

The Bill proposes a specific legislative prescription to foreign investment in agricultural land that requires more careful definition and measurement.

The Committee should note that the accompanying materials to the Bill do not suggest any significant consideration given to problem definition or to potential regulatory impact.

In terms of scope, the Bill’s focus is on defining and regulating AAL. It does not seek to address issues concerning the ownership of assets such as water rights or agricultural businesses and corporations.

7.1 New Zealand Model

The Bill makes some reliance on the foreign investment model used in New Zealand to regulate rural land. In doing so, the accompanying materials have not established whether the 5 hectare threshold used in New Zealand would be appropriate in the Australian context, whose agricultural sector differs significantly in terms of scale, composition and contribution to economic output to that of New Zealand's. Judging by the scale of agricultural activities in the two countries, it seems that the proposed threshold is too low, thus adding a relatively greater burden of regulation on foreign investment into Australia.

In adapting aspects of the New Zealand Model, the Bill also imports into the FATA an elevated degree of sensitivity for rural land which would appear to surpass that applying currently to the most significant of business proposals. Within the same piece of legislation, most business proposals and real estate applications would continue to be assessed against the FATA's 'contrary to the national interest' test, without reference to a list of prescribed criteria. This has two implications.

First, it raises concerns around incorporating in the FATA a rigid set of criteria that must be used to assess the national interest. This system can be inflexible and prescriptive. It may give rise to the future need for ongoing revisions or additions to the list of factors that make up the criteria. It has also been suggested that a statutory test could expose the Treasurer to the possibility of judicial review of his decisions as well as provide an additional avenue for opponents of a takeover to challenge it.⁴

When the Foreign Takeovers Act passed into law in 1975⁵, the associated Bill's Second Reading Speech described the intention not to prescribe national interest criteria in the following way:

I come now to the question of criteria for judging whether a foreign takeover proposal would be against the national interest. The criteria have not been incorporated into the Bill; this is because the criteria must be flexible in their interpretation and application and it has been found that it would be impracticable, consistent with the need for such flexibility, to express the criteria with the precision required by legislative form.

In practice, as noted above, the Government typically considers a range of factors when assessing foreign investment proposals and these factors are the same as those proposed in the Bill. They were published in some detail for the first time in the revised Policy published in June 2010. This has enhanced the transparency of the foreign investment screening regime.

The Bill's second implication is that it suggests the use of a dual system for the FATA in determining the national interest implications of foreign investment proposals. A key risk is that of creating confusion. Over time, the two decision making methods may be perceived to merge, particularly where investments in one area of the FATA, subject to no formal criteria

⁴ Clayton Utz, February 2011, *New foreign takeover controls on farms?*, [Online] Available: http://www.claytonutz.com/publications/news/201011/25/new_foreign_takeover_controls_on_farms.page

⁵ The Foreign Takeovers Act was amended in 1989 to become the Foreign Acquisitions and Takeovers Act (FATA).

(eg, business investments where rural land is held as assets), are similar to others that must be assessed in a different way. This may give rise to policy as well as administrative and legal difficulties. It also risks sending the perverse signal to investors in one area of business activity that investment in that area is to be discouraged.

7.2 Problem identification and data collection

The Bill's changes draw heavily on and extend the existing treatment of real estate in the FATA. Its Explanatory Memorandum and Second Reading Speech do not carry strong policy justifications for the changes.

Some media reports have suggested that rural land screening may be justified on the basis of dealing with the issue of information flows. More active screening of rural land proposals would indeed generate a flow of new data to FIRB, but it would take time for this data to be useful. The stream of rural land applications received would be incremental and would relate to new investment intentions. While statistical comparisons could eventually be possible, regulation of the kind proposed would appear to be an awkward way to tackle data gaps.

An alternative approach would be to build greater regulatory insight through improved research, analysis and information about how foreign investment is actually impacting on the agricultural sector; the extent to which foreign investment in rural land is occurring and what national interest issues arise from this investment. A better understanding of what is happening in the sector in relation to foreign investment potentially could better inform the regulatory debate. The Explanatory Memorandum to the Bill does recognise the importance of data gathering and analysis initiatives in this area, which were also recommended by the Select Committee on Agricultural and Related Industries 2010 Report into Food Production in Australia (**Heffernan**).

On 23 November 2010, the Assistant Treasurer and Minister for Financial Services and Superannuation, the Hon Bill Shorten, and the Minister for Agriculture, Fisheries and Forestry, Senator Joe Ludwig, announced a two-track process to assess the impact of foreign investment in rural land and water entitlements on the community. Under this approach, the ABS will use methodology from its agricultural census to undertake an agribusiness surveying exercise that gauges the extent of rural land and water ownership. The resultant data will also help inform a research project to be commissioned by the Rural Industries Research and Development Corporation into the role and history of foreign investment in the development of agriculture in Australia. This project will also examine the extent of foreign ownership of Australian agricultural land and the factors driving foreign investment in Australian agriculture.

7.3 Available information

While some information gaps do exist, the data that is available suggests that the current level of foreign ownership of Australia's agricultural land and water resources is low. For example, a survey of commercial broad acre and dairy farms, conducted by the Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) in 2007-08, indicates that an overwhelming majority (99 per cent) of these farms were family operated. Of the remaining 1 per cent, it is estimated that only around 0.1 per cent are foreign owned. Broad acre and dairy farms account for around 70 per cent of Australian farm businesses. Further, overall

investment in the agriculture, fisheries and forestry sector is a small part of total foreign investment in Australia, representing less than 2 per cent of approved proposals in 2008-09 made through FIRB.

It has been estimated that the ten largest landholders in Australia control approximately 52 million hectares or about 7 per cent of Australia's estimated hectare land mass and around 13 per cent of Australia's hectare agricultural area. These landholders are predominantly Australian owned or controlled.⁶

7.4 Regulatory exemptions

As indicated, one effect of the proposed changes in the Bill is to elevate the sensitivity of rural land transactions by foreign investors. An aspect of the changes that is problematic, particularly from an administrative perspective, is the position taken in the area of regulatory exemption. The existing screening arrangements applying to urban land transactions in the FATA are wide-ranging. While screening intensity can vary according to the sensitivity of the category of investment once notification occurs, foreign investors under s 26A of the FATA must compulsorily notify all interests in Australian urban land. However the Act has, for many years, provided for some specific notification exemptions via the *Foreign Acquisitions and Takeovers Regulations 1989 (the Regulations)*. The list of exemptions at Regulation 3 is lengthy. It includes carve-outs for acquisitions of real estate by charities; certain insurance and superannuation company acquisitions; bulk real estate acquisitions agreed for convenience under certificate by the Treasurer; custodial acquisitions; and certain incidental non-residential land purchases by businesses; etc. Importantly, the Regulations also exempt certain land transactions that are closely linked to the activities of Australians, such as spousal joint tenancy acquisitions and business purchases where the corporate owners are Australians but not ordinarily resident in Australia.

- The Bill would appear to specifically remove the possibility of regulatory exemption for *all* rural land transactions above the 5 hectare threshold.
- The Committee may wish to clarify whether this was indeed the policy intention of the Bill.

7.5 Privacy

Changes proposed by the Bill to the way sensitive commercial proposals must be made public, including with updates through the FIRB consideration process, are likely to raise significant privacy concerns for business and may help to undermine foreign investor confidence in the agricultural sector more broadly. FIRB has, for a long time, provided public assurances that commercial-in-confidence and personal information would be protected. There is general recognition that much of the information required to assess a foreign investment proposal would be commercially sensitive or private to the applicant. Internal FIRB procedures are in place to protect private and sensitive information in accordance with the requirements of the relevant legislation. FIRB has defended these procedures in the Administrative Appeals Tribunal.

⁶ Australian Farm Journal, October 2010, pp15-16.

7.6 Implications for Australia's international obligations

Australia is permitted to maintain its foreign investment screening regime, without being in breach of the national treatment obligations, due to certain reservations in its various free trade agreements (FTAs). However, these reservations do not specifically cover investments in AAL, nor do they permit new measures or amendments to measures that would decrease the conformity of Australia's existing foreign investment screening regime with Australia's national treatment commitments. A change to Australia's foreign investment policy resulting in less favourable treatment for foreign investors in rural land may be inconsistent with Australia's commitments under its FTAs and other instruments. These FTAs include the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) to which an Investment Protocol has been recently added.⁷ The Investment Protocol specifically provides for higher screening thresholds for New Zealand private investors,⁸ and complements broader initiatives between Australia and New Zealand towards the creation of a single economic market.

8 DRAFTING CONSIDERATIONS

8.1 Overview

The Bill contains a number of drafting issues, the more significant of which are the potential for confusion in the way AAL is to be defined and the proposed creation of a second national interest test within the same piece of legislation.

In other areas, the drafting can be problematic in places, but the problems appear largely technical in nature and could be resolved by more complete or internally consistent language. These technical gaps or issues, some more significant than others, may be inadvertent rather than intentional. The most significant of them concerns the powers of the Treasurer and notification requirements relating to AAL transactions. Some clarification of the Bill's intentions in respect of these would be helpful.

8.1.1 Definition of Australian Agricultural Land, Australian Rural Land and Australian Urban Land (Amendment 1)

As discussed, the FATA currently defines AUL as land situated in Australia that is not AAL. Australian rural land is defined in the FATA as land used wholly or exclusively for carrying on a business of primary production.

Amendment 1 introduces a new definition of Australian Agricultural Land (AAL) as being land situated in Australia that is used predominantly for carrying on a business of primary production. This distinction is problematic. It creates an obvious overlap between AAL and AUL, the latter of which is regulated differently within the FATA; AUL would not be subject to the same national interest test or publication requirements as is proposed for AAL.

⁷ The Investment Protocol to the ANZCERTA was signed by the Prime Minister and New Zealand's Prime Minister, John Key, on 16 February 2011.

⁸ The new screening threshold for New Zealander investors undertaking business acquisitions or investment in developed commercial property in Australia will increase to A\$1,005 million. The new threshold for Australians investing in significant business assets in New Zealand will increase from NZ\$100 million to NZ\$477 million. Both thresholds will be indexed annually.

8.1.2 Amendment 3 (Leases and Licences)

Section 12D of the Bill appears to be modelled on, and is very similar to s 12A of the FATA, which relates to AUL.

Subsection 12D(1)(a) does not contain an exception for a lease or licence as s 12A(1)(a) does. The effect is that all leases or licences of Australian agricultural land will be covered. This appears to make s 12D(1)(c) (which refers to leases greater than 5 years being covered) redundant. The interaction between these paragraphs could be usefully clarified.

8.1.3 Amendment 5 - Notification requirements and the power to make orders

Section 21B of the Bill similarly appears to be modelled on, and is very similar to s 21A of the FATA, which relates to AUL.

The restriction in s 21B(2)(a) that the Treasurer can only make an order prohibiting the proposed acquisition where the agricultural land is greater than 5 hectares seems inconsistent with the ability of the Treasurer to make an order directing a foreign person to dispose of an interest under s 21B(4), which is not limited to interests in AAL greater than 5 hectares. If the intention is that the Treasurer's powers only apply to acquisitions greater than 5 hectares then s 21B(4) may need to be changed to reflect this.

Likewise, the requirement to give notice under the new s 26B proposed by the Bill does not appear to be limited to applications relating to the acquisition of interests in AAL greater than 5 hectares. The result is that the Treasurer would receive notices of acquisitions of less than 5 hectares but would not be able to make an order prohibiting them. If the intention is that notices would not be necessary for acquisitions less than 5 hectares, s 26B would need to be changed to reflect this.

8.1.4 Drafting convention/correction/completeness of mention

There are a number of other examples where the Bill seeks to mirror the treatment given to AUL in the FATA in various provisions relating to AAL. This is not unreasonable in principle, given the structure of the existing legislation and the way it has provided for urban land as separate from business acquisitions. However, there are a number of instances where problems have arisen in the drafting.

8.1.5 Transitional provisions

Consideration would need to be given to whether any transitional provisions were needed in relation to the proposed amendments to the FATA.