



10 November 2020

Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Via email: economics.sen@aph.gov.au

Dear Committee Members

Thank you for the opportunity to present the minerals industry's views and recommendations on the government's *Foreign Investment Reform (Protecting Australia's National Security) Bill 2020* and *Foreign Acquisitions and Takeovers Fees Imposition Amendment Bill 2020* (the bills).

The MCA's submission to the Australian government the Treasury on 8 October 2020 (the accompanying submission) is attached to this letter. The accompanying submission presents the minerals industry's analysis and recommendations on the government's exposure draft legislation and regulations. Together these documents form the MCA's submission to the Senate Economics Legislation Committee.

The MCA recognises that one of the most important responsibilities of the Australian Government and parliament is to protect Australian citizens from threats to national security, and that the nation's foreign investment screening process plays an important role in responding to such risks.

It is also critical to Australia's economic future to maintain a competitive non-discriminatory foreign investment framework that is transparent, efficient and provides investment certainty as part of a consistent and balanced policy approach that supports the wellbeing of all Australians.

In this context, major reforms to the foreign investment framework must be designed and implemented to be proportionate and free of unintended consequences that unduly erode the national interest.

In the Prime Minister's words, 'our economic sovereignty will be achieved by ensuring our industries are highly competitive, resilient and able to succeed in a global market'.¹ This can only be achieved where domestic and national security policies are all pulling in the same direction, mutually supporting the competitiveness of Australian business and our attractiveness as a destination for foreign investment, knowhow and technological prowess.

In 2019 the resources sector earned \$289 billion of export revenue (59 per cent of Australia's total export revenue). In 2019-20 mining became Australia's largest industry with a 10.4 per cent share of the economy.

These record numbers have underpinned Australia's economic resilience through the COVID-19 pandemic as the minerals industry has sustained and created jobs in regional Australia and supported tax revenues.

¹ Prime Minister of Australia, [address to the National Press Club](#), 26 May 2020.

However, these economic benefits could not have been achieved without large capital inflows through foreign direct investment in preceding decades that helped create Australia's world-leading minerals export industry.

Access to international investment, especially foreign direct investment, remains vital to ensuring Australian mining keeps its strong comparative advantage in resources exports and continues to generate the revenues and high paying jobs needed for a sustained recovery from the COVID-19 pandemic.

The MCA's accompanying submission sets out in greater detail how, for the minerals industry, foreign direct investment (FDI) cannot simply be replaced with equivalent funding from alternative sources, such as government debt or domestic investment. There are two reasons for this. First, FDI brings with it the development of stable, long term relationships across national borders with customers that allow mining businesses to access export markets and ensure their products meet the needs of those markets. Second, FDI is the key mechanism through which technology is transferred allowing Australian mining businesses to remain at the cutting edge of productivity and global competitiveness.

While Australia's foreign investment regime is already highly restrictive by world standards, the bills and the government's broader reform package will unfortunately introduce substantial complexity and cost, creating uncertainty for a much wider range of investments. This will work to drive investment to other jurisdictions where costs are lower or market access can be assured through well-developed customer relationships.

The reforms will also work against other government priorities especially in the development of Australia's nascent critical minerals sector, which critically depends on access to technology and expertise through international investment to develop capabilities in downstream minerals processing.

Summary of key issues relating to the bills

Many of the key concepts in the government's reform package, including the definition of a 'national security business', are contained in regulatory reforms that the government proposes to introduce, and which the MCA understands continue to be refined. The MCA's analysis and recommendations on these reforms included in the accompanying submission.

Below, the MCA draws committee members' attention to the following additional comments specific to the bills that are the subject of this inquiry.

The call in power

The Explanatory Memorandum makes clear the government's expectation that call-in powers will be seldom used (about one case per year). However, with the expected 10-year period in which the call-in powers will be available to the Treasurer, the international boards that make long-term decisions to invest in the Australian mining sector need to take into account the risk of potentially adverse actions from future Treasurers in three or potentially four election cycles. In that regard, it is relevant that the call-in powers could be used to suspend acquisitions for up to 90 days while a review is undertaken, even if no adverse decision is formally reached.²

Further although exemption certificates can be applied for (at additional cost to the foreign person seeking to make an investment) there is no way to guarantee against a future use of 'call-in' powers. The Treasurer retains the power to revoke an exemption certificates granted to undertake a program of acquisitions for notifiable national security actions

Register of Foreign Owned Assets

The MCA supports the consolidation of existing registers of foreign ownership of agricultural land and water into a single register on the expectation that this will lead to a more streamlined and efficient process for registration of acquisitions.

² [Explanatory Memorandum](#), para. 1.74.

However, the register that the reforms introduce will impose a substantial additional cost and compliance burden on foreign investors. This is acknowledged by the Regulation Impact Statement, which states that it will involve around 1,800 additional registrations each year.

Costs associated with additional registrations increase not only because of registration fees – there will inevitably be increases in on internal compliance monitoring to ensure the foreign person meets their obligations to keep the register updated. For example, in relation to interests in water resources, where the volume of water or share of a water resource referred to in an interest changes a notification must be given to the register.³ Failure to give notice within 30 days of an interest changing could lead to civil penalties being imposed of up to 250 penalty units \$55,500.⁴

Streamlining less sensitive investments

The Explanatory Memorandum contemplates that the negative impacts of the reform package will be offset by the proposal to streamline less sensitive investments. Under this proposal, large institutional investment funds (for example pension funds) will no longer be treated as foreign government investors themselves simply because a foreign government investor holds a passive investment in that entity.

While this is a sensible reform that will free up large pension funds and investment houses to invest more broadly, it will not likely do much to encourage the type of investment that delivers lasting benefits to the Australian minerals industry. That is, investment from private sector firms who have the technology, intellectual property and experience to engage in joint ventures and partnerships that enhance Australia's domestic capabilities in mining and minerals processing.

Increased costs on business

The Explanatory Memorandum acknowledges that the reforms will generate additional regulatory cost for business through increased national security reviews. The estimate in the Regulation Impact Statement is that this will amount to \$1.5 million per annum on average. Inexplicably, this is an order of magnitude less than the Budget forecasts that predict government revenues will rise by \$43 million per year as a result of the measure.

In addition, the Regulation Impact Statement and Budget forecasts do not account for the true additional costs to foreign investors that will principally arise through additional legal costs and internal compliance monitoring for making applications, assessing whether applications need to be made, and administering conditions.

Summary of key recommendations

To remain competitive Australia's foreign investment review regime needs to be designed around principles of transparency, proportionality, efficiency and certainty, thereby minimising unintended consequences.

It is clear that the reforms have the potential to disrupt the international investment that the Australian mining sector relies on to support technology transfers, capacity building and mutually beneficial economic relationships across national borders.

The MCA proposes that the following options be considered to limit the impacts of the reforms on Australia's sovereign risk profile, improve investment attractiveness, and monitor the impact on investment of the reforms.

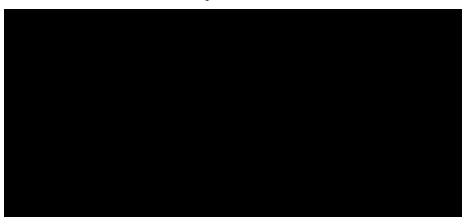
- Include provision in the legislation for a mandatory statutory review to be completed within 24 months of implementation to identify and resolve unintended policy consequences, including on:
 - The impact of the reforms on investment attraction
 - The added cost to business

³ [Explanatory Memorandum](#), para. 5.42.

⁴ [Explanatory Memorandum](#), para. 5.25.

- The effectiveness of the reforms in addressing national security risks
- The interaction of reforms with simultaneous reforms being undertaken to the Security of Critical Infrastructure (SOCl) Act 2018, and to identify areas where efficiency and transparency could be improved.
- In relation to the new National Security Test:
 - Clarify the concept of National Security Business in the proposed section 10A of the *Foreign Acquisitions and Takeovers Regulation* to make it clear that miners will not be captured by the definition simply because the raw minerals may be processed and manufactured into components that directly or indirectly feed into defence supply chains
 - Ensure the concept of 'criticality' is more clearly defined, removing the imprecise references to where the government 'seeks to influence the supply' of particular goods or services
 - Introduce a low-cost, efficient method for seeking a determination from FIRB on whether a particular business is considered a 'national security business' or land is considered 'national security land'
 - Produce clear guidance material on what is encompassed by the definition of national security business and the meaning of concepts such as 'critical'.
- In relation to the call in power:
 - Ensure the period of time available for the use of the call-in power, to be defined in the Regulation, is reduced from the proposed ten to three years
 - Provide a clear and cost effective process for investors to obtain complete protection from the use of the Treasurer's call in (at this stage, significant actions appear to be reviewable by the Treasurer under the call in powers but are not covered by the new exemption certificate in 43BB).
- In relation to fees:
 - Provide a mechanism to independently review fees and fee increases to ensure that fees and charges represent a genuine cost recovery, rather than an impost on business that amounts to a discriminatory tax on foreign investment.

Yours sincerely



TANIA CONSTABLE PSM
CHIEF EXECUTIVE OFFICER



MINERALS COUNCIL OF AUSTRALIA

SUBMISSION TO THE TREASURY ON MAJOR REFORMS TO AUSTRALIA'S FOREIGN INVESTMENT REVIEW FRAMEWORK

8 OCTOBER 2020

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EXECUTIVE SUMMARY

Foreign investment is critical to the minerals sector's ability to continue generating jobs and tax revenue and support Australia's recovery from COVID-19.

Unfortunately, the proposed Australian Government's proposed reforms to the foreign investment framework will introduce substantial complexity, uncertainty and cost to an already restrictive foreign investment regime.

The reforms would undermine other government priorities and reforms aimed at supporting a business investment-led recovery, reducing regulatory burdens and developing downstream minerals processing, including in critical minerals.

The MCA recognises that the Australian Government and parliament have a duty to protect Australia's citizens from risks and threats to national security and that the nation's foreign investment screening process plays an important role in managing such risks.

It is also in Australia's national interest to maintain a competitive non-discriminatory foreign investment framework that is transparent, efficient and provides investment certainty as part of a consistent and balanced policy approach that supports the economic wellbeing of all Australians.

This submission responds to the reform package as a whole (tranches one and two of the government's exposure draft legislation and regulations) and considers how the package impacts on the mining sector's ability to attract the foreign capital, partnerships and technologies required to develop and compete at a global level.

Foreign investment is vital

Foreign investment is a fundamental driver of economic growth in the Australian economy, enabling Australian mining companies to play their part in sustaining high paying jobs in regional areas, supporting government revenues, underpinning new growth industries and ensuring the nation remains at the cutting edge in its capability for exporting high quality commodities and services to the world.

Positive incentives to attract international investment is even more important in light of the economic shock caused by the COVID-19 pandemic and the significant global and national recovery phase that will hasten geopolitical changes, intensifying competition for resources and capital.

While the government has driven a broad domestic deregulation reform agenda to support a business-led recovery, the importance of a positive approach to foreign investment will be critical to the successful development of projects and related infrastructure that will drive the recovery and Australia's ongoing economic success.¹

The resources sector's ability to develop projects which create jobs and sustain regional communities will critically depend on access to international capital for both existing and new projects, project expansions and access to the technology and expertise needed to develop Australia's capability in downstream minerals processing.

Foreign investors must already contend with Australia's highly restrictive foreign investment regime. According to the OECD FDI Regulatory Restrictiveness Index, which benchmarks discriminatory measures affecting foreign investors (including sectoral equity limits, screening, restrictions on personnel and other measures), Australia's restrictiveness for foreign investment is more than double the OECD average. Eighty per cent of this can be attributed to Australia's existing foreign investment screening regime – well above the 23 per cent average for the OECD.

The proposed major reforms to the foreign investment framework will add to this restrictiveness and work against reforms to drive a business investment led recovery. They will substantially increase

¹ Department of Prime Minister and Cabinet, [Deregulation Taskforce Terms of Reference](#) (accessed September 2020).

complexity and investor uncertainty, shift cost and regulatory burden to investors, and involve the Foreign Investment Review Board (FIRB) in a much wider range of transactions.

The proposed major reforms also represent a structural increase in the powers available to government to intervene in the private sector, with far reaching powers being made available to the Treasurer to intervene prospectively and retrospectively in relation to actions and proposed actions of foreign investors and do not provide a clear definition on what is caught and what is not.

There is no precedent internationally for powers similar to the call in and last resort powers the government proposes, and while the precise impact on investment decisions is difficult to predict, they are highly unlikely to increase the attractiveness of Australia as a destination for foreign investment.

In the current global investment environment, where competition for capital is becoming more intense, it cannot be taken for granted that the substantial international capital flows that have underwritten Australia's economic growth for decades will continue.

The government's rationale for introducing the proposed major reforms is that they are needed to respond to increased risk to Australia's national security from developments including rapid technological change and changes in the international security environment.

The MCA supports the introduction of necessary measures to enable the Australian Government to respond to national security risks. That is an important and necessary role of government.

However, these measures must be designed and implemented to be proportionate and free of unintended consequences that unduly erode the national interest.

Recommendations

The MCA recommends that the following options be considered to limit the negative effect of the reforms on Australia's sovereign risk profile and improve investment attractiveness.

- In relation to the new National Security Test:
 - Clarify the concept of National Security Business in the proposed section 10A of the Regulation (either in Explanatory Memorandum or the regulation itself or both) to make it clear that miners will not be captured by the definition simply because the raw minerals may be processed and manufactured into components that directly or indirectly feed into defence supply chains
 - Amend the Explanatory Memorandum to better define the concept of criticality, removing the imprecise reference to where the government 'seeks to influence the supply' of particular goods or services
 - Introduce a low-cost, efficient method for seeking a determination from FIRB on whether a particular business is considered a 'national security business' or land is considered 'national security land'
 - Produce clear guidance material on what is encompassed by the definition of national security business and the meaning of concepts such as 'critical'.
- In relation to the 'call in' power:
 - Reduce the period of time available for the use of the call-in power from ten to three years
 - Provide a clear and cost effective process for investors to obtain complete protection from the use of the Treasurer's 'call in' (at this stage, significant actions appear to be reviewable by the Treasurer under the call in powers but are not covered by the new exemption certificate in 43BB).

- In relation to fees:
 - Provide a mechanism to independently review fees and fee increases to ensure that all fees and charges represent a genuine cost recovery, rather than an impost on business that amounts to a discriminatory tax on foreign investment.
- To monitor the impact of reforms on Australia's investment position:
 - within 24 months of implementation, finish a statutory review to identify and resolve unintended policy consequences, including on:
 - The impact of the reforms on investment attraction and the added cost to business
 - The effectiveness of the reforms in addressing national security risks
 - The interaction of reforms with simultaneous reforms being undertaken to the Security of Critical Infrastructure (SOCl) Act 2018, and to identify areas in which efficiency and transparency could be improved.

THE MINERALS SECTOR REQUIRES FOREIGN INVESTMENT FOR CONTINUED GROWTH

- The value of FDI in Australia's resources sector increased nearly ten-fold between 2001 and 2018, from \$36.8 billion to \$365.5 billion
- These capital inflows have seen Australian mining develop a strong comparative advantage in resources exports with massive gains for the Australian economy that have seen the resources sector generate a record \$289 billion in export revenue 2019 or 58 per cent of Australia's total export revenue
- FDI facilitates relationships with customers in Australia's export markets, stimulating innovation and the import of technology that keep mining businesses at the cutting edge of productivity
- The development of industry capabilities in downstream minerals processing, including in priority areas such as critical minerals, will only be possible where domestic policy settings and the foreign investment regime support the commercial development of a downstream industry, access to technology and expertise at terms that also support offtake by customers.
- Australia currently has a foreign investment problem with a declining share of world foreign investment and increasing competition from low cost jurisdictions. However under current policy settings Australia's foreign investment regulatory restrictiveness is well over double the average according to the OECD. This position will be made worse by the proposed policy decisions through their contribution to a lack of clarity and an increase in sovereign risk.

The ability to attract foreign investment to develop resources has been vital to the success of the Australian minerals industry.

Australia is traditionally a net importer of capital, requiring foreign investment to fill the gap between domestic savings, debt and capital investment. This capital shortfall has consistently been around 4 per cent of GDP.² Without international investment, Australia would need to take on additional debt or forgo the revenue inflows and jobs generated by investment in productive capacity.

While portfolio investment and debt finance are important sources of investment in the mining sector, it is foreign direct investment (FDI) that brings the most substantial benefits. This is because FDI is characterised by a substantial commitment from the investor (in contrast to debt finance and portfolio investment which can be recalled relatively quickly). This leads to the formation of long term, stable partnerships, collaboration on complementary technologies and the research and development of new and innovative ways to resolve challenges.

FDI leads to spill over benefits to the Australian economy through the creation of new employment opportunities as well as facilitating productivity and capacity building through technology, skills and innovation transfers, financing infrastructure and opening up access to global supply chains and markets. Australian mining has generated entire new export industries in the mining, equipment, technology and services (METS) sector with a wide variety of dynamic METS businesses now making a substantial contribution to the Australian economy.

In the last few decades Australia benefited from very high inflows of capital into mining driven by foreign direct investment. The value of FDI in Australia's resources sector increased nearly ten-fold between 2001 and 2018, from \$36.8 billion to \$365.5 billion.

These capital inflows have seen Australian mining develop a strong comparative advantage in resources exports with massive gains for the Australian economy. In the 2019 calendar year

² A McKissack and J Xu, Commonwealth Treasury, Treasury Working Paper No. 2016-01, p. 10.

resources accounted for 58 per cent of Australia's total export revenue, a record high of \$289 billion generated by the 1.1 million employees working directly and indirectly in the mining and METS sectors with many located in regional Australia.

These remarkable figures could not have been achieved without competitive policy settings which attracted foreign investment in the infrastructure, productive capacity, skilled workforce and technical expertise required to support Australia's export industries.

This investment created the opportunity and the infrastructure to efficiently produce the range of bulk materials required by the growing economies in our region.

The range of commodities and materials required by new technologies is changing as economies develop. Australia's ability to respond by supplying new minerals and capturing the economic benefits of mining and downstream processing will depend on access to foreign direct investment, the technology access that this enables and the ability to compete with other countries with existing downstream processing capabilities throughout start-up, construction and ongoing operational phases.

International investment stimulates technology transfers between home and host countries

The benefits of international investment extend much further than their dollar value. The Australian economy has benefited significantly from foreign direct investment that has supported the import of advanced technologies as a foundation for new industries in Australia.^{3 4}

Most (if not all) of Australia's downstream minerals processing industry is based on foreign investment that has transferred privately held intellectual property and knowledge to Australia together with large inbound capital flows required to establish, adapt and use technology and associated infrastructure.

- Examples of this include:
- The establishment of the alumina and aluminium industries
- The current investment wave developing new lithium hydroxide processing facilities
- The establishment of Australia's first rare earth elements mine and concentrator.

Even greater international investment and knowledge transfer will be needed if government policy is directed at the establishment of new domestic capabilities in rare earth element refining and processing downstream battery and new technology mineral production to enable Australian companies to keep pace with leading edge technology developments.

In many cases, the international developers of these technologies are investing in Australia, thereby building a bigger and stronger METS industry. Major software companies such as Microsoft, IBM and Dassault are making major investments in local offices that not only transfer their technologies to Australia but spur new research hubs as local start-up companies look to collaborate with them.

Open investment together with collaboration between governments and industry is the foundation of these technology transfers and essential to the future growth of Australia's mining and METS sector as well as the collective aspirations of industry and government to move into higher value-adding downstream processing.

³ OECD Paper, Growth, Technology Transfer and Foreign Direct Investment, OECD Global Forum on International Investment, November 2001.

⁴ Department of Foreign Affairs and Trade, [Benefits of Trade and Investment](#), (accessed September 2020).

Box 1: FDI facilitates cooperation delivering mutual benefits

The Carbon Transport and Storage project is an ongoing collaboration between Glencore's Carbon Transport and Storage Company, InterGen's Millmerran Power Station and the Huaneng Clean Energy Research Institute. This project will demonstrate an entire CCS supply chain using proven Chinese carbon capture technology at an Australian power station and safely storing it in Queensland's Surat Basin.

The Australia–China Joint Coordination Group (JCG) fosters research collaboration, technology development, data exchange and networking between Australia and China. Since 2007 the JCG has delivered projects that have made a major contribution to improving the economic and environmental performance of coal use globally. Projects within the JCG have included:

- The Australia-China Post Combustion Capture Study. This focused on the economic and technical feasibility of an industrial scale Carbon Capture and Storage (CCS) project in China. This project has subsequently provided a significant depth of knowledge on low emissions fossil fuel technologies, reducing deployment costs and risks in Australia and China.
- The China Australia Geological Storage (CAGS) project. This has provided an important international forum for Australia and China to cooperate on advancing and promoting carbon storage technology. CAGS has provided an invaluable avenue for Australian and Chinese researchers to visit each nation's low emission technology facilities and build intellectual capital.

These projects demonstrate the deep relationships and mutually beneficial collaborations that develop across national boundaries, leading to innovation that drives more productive and efficient businesses and improves Australia's competitive strengths.

Australia is often regarded as a world leader in mining technology that includes geoscience, ore extraction, mineral processing, bulk transportation and environmental management. While there has been significant R&D investment in these areas, Australia is not alone in these endeavours.

The Australian mining industry's source of competitive advantage is its capacity as a technology developer and technology adopter. Its ability to partner with technology leaders and investors across the world has led to the development of automated infrastructure networks, exploration methods enhanced by artificial intelligence, new safety systems for protecting workers and improved environmental management. These innovations have increased the productivity and safety of the Australian mining industry.

FDI is one of the keys to downstream minerals processing in Australia

The Australian Government has identified the exploration, extraction, production and processing of critical minerals as a strategic priority.⁵ While many of the rare earth metals of interest are in abundant supply and capable of being extracted, the limitation is that projects for beneficiation – including separation, processing, refining and smelting – face challenges in attracting the foreign investment needed to develop them in Australia. The issue of supply chain concentration, the seat of security of supply concerns in this area, is one of who controls the offtake rather than who controls the mine.

There are a range of factors impacting on Australia's capacity to attract investment in downstream processing, refining and smelting. The cost of inputs such as energy is a major factor as is access to the necessary technology.

Access to technology in a way that enables its early adoption requires foreign direct investment.

⁵ Australian Government, *Australia's Critical Minerals Strategy*, 2019.

Innovations in downstream minerals processing happen regularly. While Australia has at times led the world in mineral processing innovations, it still relies on imported technologies.

Foreign Direct Investment by the owners of intellectual property is a key mechanism for importing technology to Australia and one that will be essential for meeting the government's recently announced priorities for developing a domestic 'green steel' industry.

The race to develop low-carbon steel production methods is being led by two competing technologies. The first is the hydrogen-based Hybrit method being developed by a Swedish joint venture between SSAB, LKAB and Vattenfall.⁶ The second is an electrolysis method, similar to aluminium smelting, being developed by Boston Metals in the US.⁷

For Australia to be an early adopter of either of these competing technologies and producer of green steel, it will need to attract investment from the foreign-based owners.

An open and transparent foreign investment regime is essential to achieving this technology transfer.

Australia's capacity to build a downstream processing industry for critical minerals is inextricably linked to the ability to attract and adapt the technology needed for downstream processing new technology and critical minerals such as lithium including refining, cracking and smelting required for rare earth minerals.

Box 2: How international investment transformed the lithium industry in Australia

The flow of international investment has transformed the lithium industry in Australia. Whereas Talison Lithium had previously focused on extracting and concentrating spodumene for export, Tianqi and Albemarle were experienced chemical producers who brought their technologies for the production of lithium hydroxide to Australia.

By 2017 both Albemarle and Tianqi were developing plans to invest in large-scale lithium hydroxide manufacturing in WA. Both have since made final investment decisions, and Tianqi has finished construction on its first train in Kwinana, Albemarle's first train near Bunbury is nearing completion. Both sites have plans for significant expansions as world lithium demand grows.

These investments in a downstream processing industry and the necessary technology would not have been possible without supportive foreign investment policy settings.

A similar dependence on investment and access to technology can be seen in the emergence of aluminium and other smelting operations in Australia's industrial past.

An open clear and certain investment environment and collaboration between governments and industry is the foundation of these technology transfers, and essential to the future growth of any higher value-adding downstream processing industry.

As proposed, the reforms will increase investor uncertainty and risk in the critical minerals sector. Increasing the barrier to foreign direct investment will severely limit the potential to harness cutting edge technologies through FDI and undermine any attempt to establish downstream processing in Australia.

Australia currently has an investment problem

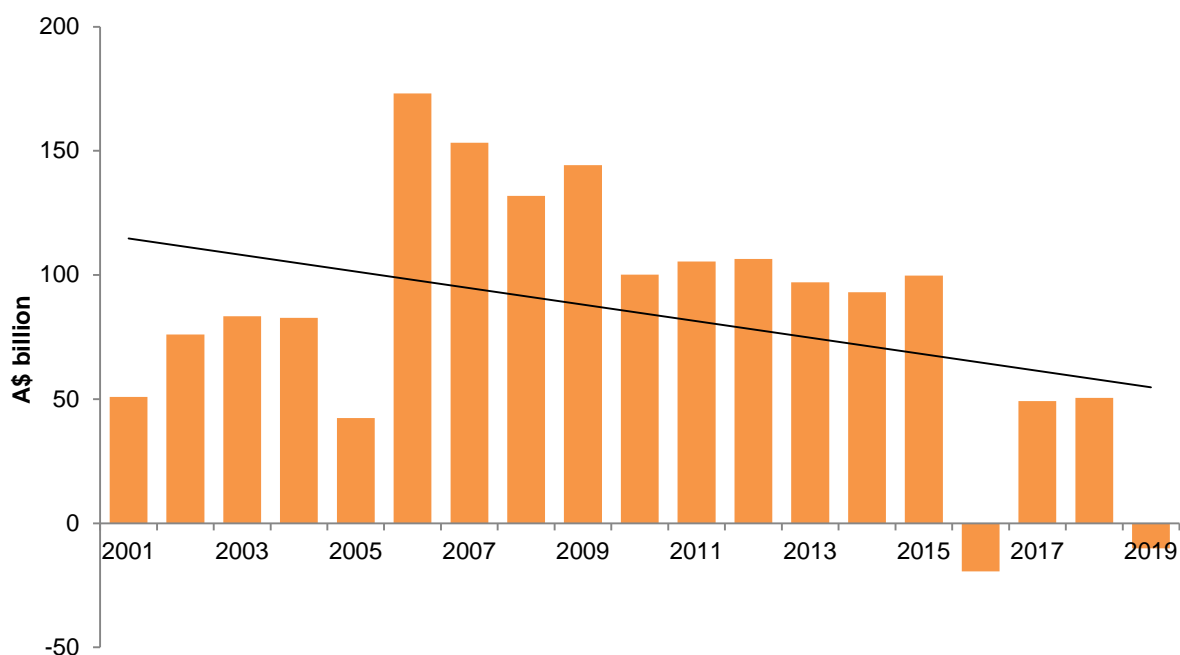
Business investment in Australia has been declining for some time (particularly non-mining business investment). This has manifested as a slowing in the growth rate of our capital stock (or capital

⁶ Hybrit website, www.hybritdevelopment.com, accessed 1 October 2020.

⁷ Boston Metal website, www.bostonmetal.com, accessed 1 October 2020.

deepening), which is flowing through to lower labour productivity growth and the low wage growth Australia has experienced over the past decade.

Chart 1: Annual foreign investment into Australia (A\$ millions)



Source: ABS cat no. 5352.0 - International Investment Position, Australia: Supplementary Statistics, 2019; table 1

Australia's share of world foreign investment has been trending downwards since the 1980s. While Australia is still an attractive place to do business, competition for investment has grown. This is reflected in the Fraser Institute's Annual Survey of Mining Companies, which shows the investment attractiveness of emerging mining regions in South America and Africa has been rising relative to Australia.

Australia already has one of the most restrictive foreign investment regimes in the world

Australia already has high barriers to foreign direct investment (FDI) compared to other OECD countries. The OECD's FDI Regulatory Restrictiveness Index indicates that in 2019 Australia was more than twice as restrictive for foreign investment as the OECD average.⁸

Moreover, analysis of the OECD data makes it clear that, in Australia's case, screening and approval mechanisms are responsible for the majority of Australia's overall foreign investment restrictiveness, as opposed to other types of restrictiveness measured by the index (equity restriction, key foreign personnel and other restrictions).

The data indicates that on average the screening and approval mechanisms in OECD countries represent 23 per cent of overall restrictiveness. By contrast, 80 per cent of Australia's foreign investment restrictiveness can be attributed to the nation's current screening regime, according to the OECD.⁹

The material effect of the foreign investment screening regime has also been observed by the Productivity Commission. The commission has noted that while rejection rates may be low, the screening regime can discourage investors from applying at the outset, or cause them to pre-emptively withdraw applications.¹⁰

In effect, the amendments to the regime as proposed will compound this issue rather than ease it.

⁸ OECD, [FDI restrictiveness index](#), 2020.

⁹ MCA calculations based on data from OECD FDI Regulatory Restrictiveness Index.

¹⁰ Foreign Investment in Australia, p. 12.

In addition to the *Foreign Investment and Takeovers Act* further regulatory burdens have been imposed in recent years including under the *Register of Foreign Ownership of Water or Agricultural Land Act 2015 (Cth)*.

This Act requires foreign persons to notify the Australian Tax Office (ATO) of acquisitions in certain property rights, including acquisitions of registrable water entitlements that are commonly attached to mining exploration leases.

Recent foreign investment screening decisions have highlighted how government intervention through the foreign investment review process may not be sensitive to current economic conditions, leading to inconsistent market signals.

Box 3: Expanded assessment timeframes and a lack of clarity on approvals and coverage undermines investor interest in Australian projects

Alto Metals Ltd (Alto) is a gold exploration company with a gold project located 600km north of Perth in the East Murchison Mineral Field of Western Australia.

On 21 February 2020 Goldsea Australia Mining Pty Ltd, a wholly-owned subsidiary of Shandong Goldsea Group Co Ltd announced its intention to make an off market takeover offer for Alto Metals Limited valued at approximately \$20.7 million. A formal offer was announced on 24 March 2020.

Alto's directors unanimously recommended that its shareholders accept an improved offer on 1 May, describing the offer as 'an attractive opportunity to realise value for their investment in cash, particularly in light of the uncertainty seen in the current global equity markets and the requirement that Alto would need to raise immediate capital in the near term to fund exploration and working capital.

The offer was conditional on Goldsea receiving FIRB approval. Goldsea agreed to a voluntary one-month extension until 27 May 2020, to enable FIRB to continue its process given the increased workload associated with the reduced thresholds.

On 24 June 2020 Goldsea announced that the FIRB had requested a further extension of six months to consider Goldsea's application, and had been unable to provide Goldsea with any details for Goldsea to confirm this extension was required in the context of Goldsea's application.

Given the extension would mean the window for a FIRB decision extended to 10 months, Goldsea withdrew its application and announced its intention to allow the takeover offer to lapse.¹¹

Investors assess the range of factors that enable them to rank potential projects on a risk adjusted rate of return basis. The potential investment and first mover benefits associated with a new area of investment and the application of a proprietary technology can be quickly outweighed by the negative impact of risk and uncertainty.

This sovereign risk is exacerbated where regulatory frameworks raise the potential for regulatory decisions with material and retrospective changes, including forced divestiture.

¹¹ Goldsea Group, Press Release, '[Goldsea's all-cash takeover bid for Alto – intention to allow offers to lapse](#)' 24 June 2020.

CONSIDERATION OF THE REFORM PACKAGE

- To remain competitive Australia's foreign investment review regime needs to be designed around principles of transparency, proportionality, efficiency and certainty, thereby minimising unintended consequences
- The proposed reforms:
 - Amplify the existing complexity in the regime by adding new layers of regulation that do not give investors clarity on whether or not notification to FIRB is required
 - Will through unintended consequences drive investor uncertainty, costs and compliance burdens.

The following reform options should be considered to limit the impacts of the reforms on Australia's sovereign risk profile and improve investment attractiveness:

- In relation to the new National Security Test:
 - Clarify the concept of National Security Business in the proposed section 10A of the Regulation (either in Explanatory Memorandum or the regulation itself or both) to make it clear that miners will not be captured by the definition simply because the raw minerals may be processed and manufactured into components that directly or indirectly feed into defence supply chains
 - Amend the Explanatory Memorandum to better define the concept of criticality, removing the imprecise reference to where the government 'seeks to influence the supply' of particular goods or services
 - Introduce a low-cost, efficient method for seeking a determination from FIRB on whether a particular business is considered a 'national security business' or land is considered 'national security land'
 - Produce clear guidance material on what is encompassed by the definition of national security business and the meaning of concepts such as 'critical'.
- In relation to the call in power:
 - Reduce the period of time available for the use of the call-in power from ten to three years
 - Provide a clear and cost effective process for investors to obtain complete protection from the use of the Treasurer's call in (at this stage, significant actions appear to be reviewable by the Treasurer under the call in powers but are not covered by the new exemption certificate in 43BB).
- In relation to fees:
 - Provide a mechanism to independently review fees and fee increases to ensure that fees and charges represent a genuine cost recovery, rather than an impost on business that amounts to a discriminatory tax on foreign investment.
- To monitor the impact of reforms on Australia's investment position:
 - Within 24 months of implementation complete a statutory review to identify and resolve unintended policy consequences, including on:
 - The impact of the reforms on investment attraction
 - The added cost to business
 - The effectiveness of the reforms in addressing national security risks

- The interaction of reforms with simultaneous reforms being undertaken to the Security of Critical Infrastructure (SOCl) Act 2018, and to identify areas where efficiency and transparency could be improved.

To remain competitive Australia's foreign investment regime needs to be designed around principles of transparency, proportionality, efficiency and certainty

Any policy, legislative or regulatory reform should consider how changes will deliver its intended objectives and how it will minimise unintended consequences. Individual reforms and the interactions between the reformed elements of the regime should be assessed carefully to ensure that the regime does not increase the complexity, uncertainty or cost (above cost recovery) for investment approval in Australia.

The arrangements for the existing national interest test remain in place. The opportunity for reform of this test to enhance transparency, specificity and certainty, thereby reducing the potential for associated unintended consequences, has not been pursued meaningfully.

While the cost of some applications has gone down, the overall financial cost on the total pool of investment applications has gone up. This is because the uncertainty created for investors in those projects that may or may not be caught under the definition of national security business has increased the need to apply for review under the review process.

For any emerging industry or mining sector – which, by definition, is already assessed as higher risk by investors – an increase in sovereign risk will add to commercial and economic incentives to direct investment into other opportunities. The impact on access to technology and the ability to grow downstream value added industries in Australia cannot be understated.

The Productivity Commission recently identified a number of areas in which the operation of the national interest test could be improved to facilitate more investment, stating that there are 'unnecessary costs associated with the design of the national interest test, the use and enforcement of conditions, and poor transparency'.¹²

In particular, the Commission recommended the test be narrowed to exclude those risks that can be mitigated through national regulations such as competition, and that tighter policy guidance be provided around issues to be considered in screening.

As the Commission noted, the principles of good regulatory practice are well-established and the OECD has outlined how these principles apply to investment policies in relation to national security. In particular, policies should be based on non-discrimination, transparency and predictability, regulatory proportionality and accountability.¹³

Foreign investment requires transparent review criteria and processes that signal Australia is open for business and will provide a fair opportunity to proceed with a project before investors commit to even early stages of mineral projects such as exploration. In comparison, opaque reviews based on national security are likely to limit investor interest and provide no tangible benefit to Australia when the resources remain undeveloped.

The optimal approach to ensuring a single country cannot control the supply of a resource in Australia is to ensure many countries are interested in developing multiple projects that deliver alternative choices of supply. An open and transparent foreign investment review process is the best way to deliver this supply while maximising the economic benefits to Australia.

¹² Productivity Commission, [Foreign Investment in Australia](#), Commission Research Paper, Canberra, June 2020, p. 81.

¹³ Ibid p. 19.

The reforms make an already complex regime even more complex – and widen it to a larger number of investors

Australia's current foreign investment regime requires foreign persons seeking to invest in Australia to consider whether the proposed actions they will be engaged in are either 'significant actions' in which case the investor may voluntarily notify the Foreign Investment Review Board (FIRB) of the relevant action, or 'notifiable actions' in which case the action must be notified to FIRB.

These tests are complex and layered, varying depending on whether the foreign person is a foreign government investor or a private investor.

The proposed reforms will amplify the existing complexity by introducing three new layers of regulation that investors will need to deal with to ensure they are not captured by the regime. These are:

1. Whether the proposed actions amount to a 'notifiable national security action' (the national security test)
2. Whether an action or proposed action amounts to a 'reviewable national security action' (the call in power), and
3. Assessing the risk of whether the 'last resort power' may be triggered in the future.

The absence of monetary thresholds for the new tests removes one of the key balances in the current regime. The advantage of monetary thresholds that apply to notifiable actions is that they provide clarity and certainty to foreign persons on which transactions require FIRB notification, without an assessment needing to be made against a complex definition.

The application of the new tests will inevitably lead to an increase in the types of transaction that require costly legal assessment against the less precise definitions encompassed by the concepts of 'national security business' and 'national security land'.

As can be seen in the charts in Appendix A, this represents a substantial increase in complexity for investors who could previously be satisfied on the basis of the thresholds that they were not required to notify FIRB of a transaction.

The new regulatory structure will make it difficult for an investor to be satisfied that there is no need to notify FIRB about a proposed transaction. In order to do so, the investor will need to be satisfied that they do not fall under at least four separate tests ('significant action', 'notifiable action', 'notifiable national security action' and/or 'reviewable national security action') after which the investor will still be exposed to risks of the use of the last resort power. This will send a policy signal to prospective investors that every transaction should be notified regardless of value or potential risk to national security.

The new national security test

The introduction of the new zero-threshold national security test and associated definition of a National Security Business, as currently drafted, creates significant uncertainty as to the types of businesses that may be covered.

The inclusion of businesses that develop, manufacture, or supply, critical goods or technology for (or intended for) a military end-use by defence and intelligence personnel or the defence force of another country could be interpreted very widely to include any potential input to a defence supply chain.

Given that minerals companies produce raw materials that are ubiquitous and used in all types of consumer and military goods, it is likely to be unclear to investors making even very small investments where this definition begins and ends.

While a community of practice will likely develop among the legal practitioners that work closely with the foreign investment review board, over time clarifying aspects of the concept of national security

business, the costs of accessing specialised legal advice where none was previously required will present an additional cost and barrier to investment.

The Explanatory Memorandum casts some light on concept of 'critical', which makes it clear that it encompasses more than goods, technology and services that are essential to the core capabilities of defence and agencies in the national intelligence community. Criticality extends to 'sensitive goods, technologies and services of which the Australian Government seeks to influence the supply as a matter of national security'.

The Explanatory Memorandum appears to contemplate that 'criticality' will be informed by fluid policy decisions of government with the concepts of national security business and national security land capable of expansion in a number of ways, such as:

- Goods being added to defence related policy documents such as Defence Industry Policy Statement, Defence Industrial Capability Plan, and the Defence and Strategic Goods List
- The Australian Government altering its strategy in relation to critical minerals strategy in a way that could be interpreted as seeking to influence the supply of particular minerals that were not previously targeted
- Expansion through incoming reforms to the *Security of Critical Infrastructure Act 2018*¹⁴
- The Treasurer may add land to a register by legislative instrument.

Because the definition can be expanded through policy changes there is an added risk that a point in time assessment made prior to a proposed transaction may become inaccurate after the investment is made.

Investors are generally not well positioned to assess matters of defence priority and they (and their legal advisers) will likely be inclined to take a risk-averse approach. Ultimately this will decrease the risk-adjusted rate of return of an investment and reduce the investment's ranking against other opportunities.

The MCA notes the inclusion of an exemption certificate under the proposed sub-section 43BA of the Regulation, which appears to provide protection from the application of the new national security test. While this is a welcome addition, this will add costs that will amount to 75 percent of a 'notional fee amount'. This could be interpreted as an attempt to harvest the potential for revenue created by uncertainty in the regime's application and the increase in sovereign risk it generates.

The MCA recommends that the government consider ways to introduce more clarity and certainty to the new concepts proposed to be introduced, for example:

- Reconsidering the introduction of monetary thresholds for the new tests
- Amending the explanatory memorandum to better define the concept of criticality, removing the imprecise reference to where the government 'seeks to influence the supply' of particular goods or services
- Introducing a low-cost, efficient method for seeking a determination from FIRB on whether a particular business is considered a 'national security business' or land is considered 'national security land'
- Producing clear guidance material on what is encompassed by the definition of national security business and the meaning of concepts such as 'critical'.

The onus for assessing whether a proposed investment is captured by the new national security test rests on the prospective investor.

¹⁴ Department of Home Affairs, Consultation Paper, [Protecting Critical Infrastructure and Systems of National Significance](#), August 2020.

Given that the reforms also incorporate significant increases in penalties – up to ten times as high as previously – there are potentially severe consequences if the investor does not notify voluntarily.

The increase in sovereign risk has the potential to slow the development of new small and medium mining operations by slowing the availability of capital, research and access to leading edge technology.

The government should reduce the sovereign risk for mining related investment to as low as practicable. This includes focusing the interpretation of criticality in minerals to the ownership structure of offtakes rather than mining itself.

Continued restrictions to investment in Australia will result in a faster development of alternative supplies globally at the expense of the Australian taxpayer, worker and mining sector. A carefully structured regime will support the development of downstream processing capacity and related economic benefits while ensuring that offtake arrangements manage the supply chain risks associated with concentrated ownership structures.

The new call in power

Under the new call-in power, the Treasurer will be able to review a 'significant action' or a 'reviewable national security action', enabling the exercise of powers of prohibition or disposal if the Treasurer considers that the action poses a national security concern.

Either all mining should be exempt from the call in power or the majority should be excluded (including mineral sands). Substantial work is required to further develop and refine the exemption certification mechanism to mitigate the sovereign risk faced by mining activities (i.e. where a case can be made that a critical mineral or defence supply chain could reasonably be threatened).

The MCA is comforted by the Explanatory Memorandum's statement that the government expects that the overwhelming majority of investments will not be called in for review. There is no guarantee however that these far-reaching powers available to the Treasurer will not be used with a contingent negative impact on the investor's perceived risk.

This does not provide a welcoming signal to investors looking to make long term investments in projects with significant sunk capital and long revenue lead times.

The inclusion of a 10-year time limitation on the exercise of the Treasurer's power to undertake a national security review within the time prescribed by the regulations is an important limitation. However the MCA's view is that this should be reduced to 3 years, given that the last resort power is available to deal with subsequent national security risks that may emerge.

The MCA welcomes the introduction of a new exemption certificate category under the proposed section 43BB of the Regulations. The MCA understands that the 43BB certificate will provide protection for investors from being called in for review if 'reviewable national security actions'.

However, since 'significant actions' can also be called in, it is unclear whether the exemption certificate provides a complete protection, or whether more than one exemption certificate would need to be applied for. The coverage of the exemption certificate in section 43BB of the Regulations should therefore be widened.

It is clear that the broad discretion of the Treasurer to review investments will lead many investors to seek certainty by voluntarily notifying the proposed action to the Treasurer. Given ambiguity on when the new national security may come into play and the absence of monetary thresholds for that test, exemption certificates could become a significant added cost for investors both in terms of the fees themselves and the associated legal fees for navigating the regime.

The new last resort power

The proposed 'last resort' review power will give the Australian Government the ability to reassess approved foreign investments where a subsequent national security risk emerges. Where such risk cannot be otherwise mitigated, orders can be made to force divestment.

These are welcome inclusions, along with the requirement that the Treasurer must be satisfied that the use of other options under existing regulatory systems would not adequately reduce the national security risk.

The MCA recommends that consideration be given to an additional limitation to the exercise of the power that the minimum amount of intervention be made to mitigate the national security risk. For example, the government would be required to consider whether the imposition of a condition would be sufficient before using the power to order divestiture, and to provide reasons which could be subject to appropriate judicial review processes.

However limited, the existence of a power of divestment is likely to increase sovereign risk. The existence of the power and ambiguity on when it might be used means investors making any investment will need to consider making a pre-investment notification.

This will likely drive a substantial increase in the FIRB's workload, and increases in red tape and costs as investors seek protection from the risk of regulatory intervention. Making voluntary notifications in order to protect against the commercial risk of the Treasurer's power to call in an investment action for review may be a perverse outcome –creating an additional regulatory burden and slowing down FIRB approvals even further.

Evaluation of aspects of the package that may be beneficial to investment in the mining sector

The reforms include a number of positive developments that are improvements on the existing system from the perspective of investors in the mining sector, including:

- Exemption for mining and production tenements: the proposed section 27A of the Regulations will provide an exemption from the operation of the Act where an interest acquired is a revenue stream in a mining or production tenement where the revenue stream does not entail rights to occupy land
- Exemption for exploration tenements: the proposed section 27B of the Regulations will provide an exemption from the operation of the Act where an interest in an exploration tenement is acquired by a foreign person (who is not a foreign government investor).

The limitation is noted that these exemptions do not apply where the tenement is acquired in respect of Australian land that is national security land, or a national security business. The proposals will however remove the uncertainty in the existing regime on whether a grant of a royalty or investment into exploration licences amounts to an interest in land requiring foreign investment approval.

The new Register of Foreign Ownership of Australian Assets

In the first tranche of reforms the government announced a new Register of Foreign Ownership of Australian Assets, administered by a registrar appointed by the Treasurer. The new register will remain confidential, however reports will be provided to Parliament.

The register imposes obligations on foreign persons to notify the registrar if the person begins to hold an interest in Australian land, water or an Australian entity or business (including if there is a change in nature of such an interest or the person ceases to hold the interest). This will require ongoing compliance monitoring as a standard process for inbound investors.

The reporting requirements are also potentially duplicative, adding to the requirements that already apply when reporting to the Australian Tax Office for the two existing registers of foreign interests in agricultural land and water rights. It is unclear from the regulations whether there will be any streamlining of reporting to ease the compliance burden on investors.

In previous submissions, the MCA has noted that the minerals industry accesses and uses water differently to other industries, and that water access is largely non-tradeable.¹⁵ The same concerns about the potential for generalised reporting of water entitlements may lead users of the information to assume that all water entitlements are 'owned', tradable, consumed and be of a type suitable for agriculture or even domestic purposes, which for the minerals industry is not the case. These exemptions should therefore be applied along the lines of previous recommendations.

Fees and Penalties

The draft legislation and regulations set out a new framework for foreign investment fees. The amendments make it clear that 'all fees imposed are a tax' and do not necessarily reflect a fee for service.¹⁶

The reforms to fees represent an almost five-fold increase in the maximum fees payable for transactions, increasing the fee cap from \$107,100 to \$500,000. Fees will also hit a wider range of small transactions, introducing new fees for:

- Starting an Australian business or a national security business (\$2,000)
- Acquiring a direct interest in an entity or Australian business (\$1,650 to \$125,000)
- Where there is a notification of an acquisition of a direct interest in a national security business, where no notification was previously required.

While medium sized transactions of \$10 to \$100 million will benefit from lower fees, cost increases will be felt most acutely at the lower end of the scale. For example, acquisitions in commercial land costing less than \$10 million will attract a fee more than three times higher than the current fee.

The cost of new exemption certificates for notifiable national security actions and reviewable national security actions is no longer a flat fee, but will be calculated at 75 per cent of the fee for seeking a no objection notification. This means that an exemption certificate could potentially cost more than 10 times as much as the \$36,900 chargeable under the current regime.

In combination with the uncertainty and wider reach of the regime, the increase in many of the fees that will be chargeable and the new framework providing more triggers for the payment of fees is likely to represent a substantial increase in cost for inbound investment.

Australia's reputation as an attractive destination for investment and keep investment costs down would benefit from foreign investment fees being subjected to regular independent review on the basis that they should represent a genuine fee for service as opposed to a tax.

¹⁵ MCA, submission on the draft register of foreign ownership of water or agricultural land draft rules, 2 March 2017.

¹⁶ Draft Explanatory Memorandum to the *Foreign Investment Reform (Protecting Australia's National Security) Bill 2020*, p. 91.