

Chapter 5

Evidence in support of change to the legislative or regulatory framework

5.1 This chapter considers evidence to the committee which raised concerns regarding the current regime and supports a change to the framework on the basis of economic, national security and national interest factors.

Economic considerations

5.2 A number of submitters to the inquiry suggested that the lease of the Port of Darwin raised questions about the long term consequences of allowing critical infrastructure to be either owned or leased by private sector actors.

5.3 In its submission, Victoria University's Institute of Supply Chain and Logistics maintained that the Port of Darwin lease highlighted the potential economic consequences of allowing foreign-owned interests to acquire controlling stakes in Australian land, infrastructure assets or companies:

Further research conducted by the Institute indicates that the general public may not be fully aware of the extent and ramifications of this shift in ownership in businesses that are critical to Australian trade. The main driver for overseas owners is to maximise return on the considerable investment that they have made to acquire assets, with perhaps little concern or knowledge of what is best for Australia's interests...A number of ports...have increased their service charges substantially since being privatised. As these ports have a monopoly position in servicing their hinterland, port users have no choice but to pay these increased charges in order to get their products to and from the port.¹

5.4 Dr Gennadi Kazakevitch, Deputy Head of the Economics Department at Monash University, also highlighted the potential consequences of allowing foreign investors to acquire significant holdings in Australian companies or infrastructure. Dr Kazakevitch argued that the current foreign investment review process does not adequately consider the governance arrangements of foreign-owned firms seeking to invest in Australia.² Dr Kazakevitch maintained that the framework does not sufficiently examine the extent to which a foreign government might be in a position to influence (directly or indirectly) the commercial decisions of a foreign company that owns or operates a business in this country:

Particularly, the 1975 Act does not imply [sic] the FIRB to look into the proportion of foreign government ownership in such a company; involvement of a foreign government in a company's decision making (particularly, through the government's representation on the FIRB of directors); taking government's orders that limit a company's commercial

1 Victoria University, Institute for Supply Chain and Logistics, *Submission 3*, p. 2.

2 Dr Gennadi Kazakevitch, *Submission 5*, p. 2.

independence, or complying with legislations [sic] beyond the ones that normally regulate commercial decision making.³

5.5 These submitters suggested that the current foreign investment review framework requires amendment to address some of the potentially significant economic and political consequences of foreign direct investment in the Australian economy.

5.6 The Maritime Union of Australia (MUA), in a submission to the Northern Territory's Legislative Assembly select committee inquiry, argued that any investment in the Port of Darwin by a private operator will disadvantage some port users. In particular, the MUA questioned the ability of the Australian Competition and Consumer Commission (ACCC) to intervene effectively in any dispute between port users and a private port operator.⁴

5.7 According to the MUA, the arguments in favour of the lease of the Port of Darwin neglected the real-world record of private port operators' investment strategies. It cited the case of Flinders Ports, the private operator of Port Adelaide. The MUA alleged that, while Flinders Ports has made a number of significant investments in Port Adelaide's infrastructure, it has done so in an unbalanced and potentially anti-competitive manner.⁵

5.8 By using its substantial profits from the operation of the port to expand into stevedoring services, the MUA suggests that Flinders Ports has become, in effect, a landlord and a competitor to those companies, such as Patrick and Qube, which also provide stevedoring services at Port Adelaide. According to the MUA, this 'dual' position leaves the door open to infrastructure investment that unfairly advantage the subsidiary companies that are owned by the port operator:

Flinders Ports does have a better record of investing in port infrastructure [compared with other private port operators]. However, the logic of privatisation does mean that investment appears to have been made in an unbalanced way that disadvantages other port users...One result of the expansion of Flinders Ports into stevedoring is that it is effectively both a landlord and a competitor to Patrick and Qube. The ACCC warns against such an outcome in ports.⁶

5.9 Although the NT Government suggested that the ACCC could act as a final arbiter in any dispute between the port operator and the port user, the MUA cast doubt

3 Dr Gennadi Kazakevitch, *Submission 5*, p. 2.

4 Maritime Union of Australia, *Submission to the Port of Darwin Select Committee, Legislative Assembly of the Northern Territory*, 11 March 2015, p. 2, http://www.nt.gov.au/lant/parliamentary-business/committees/pod/Submissions/Number_3_Maritime_Union_of_Australia.pdf (accessed 9 December 2015).

5 Maritime Union of Australia, *Submission to the Port of Darwin Select Committee, Legislative Assembly of the Northern Territory*, 11 March 2015, p. 17.

6 Maritime Union of Australia, *Submission to the Port of Darwin Select Committee, Legislative Assembly of the Northern Territory*, 11 March 2015, p. 17.

on this contention. It cited a recent ACCC analysis of stevedoring at Australian ports, *Container Stevedoring Monitoring Report – October 2014*.⁷

5.10 In that report, the ACCC made clear that ports, largely by virtue of their nature as major pieces of critical infrastructure, are usually monopoly or near-monopoly assets. This provides their operators with considerable market power.⁸ The ACCC recommended that any government planning to privatise a major piece of critical infrastructure, whether on the base of a long-term lease or an outright sale, must construct a regulatory framework that does not attempt to make the asset more attractive to a potential buyer. In particular, the ACCC took the view that a price monitoring mechanism does not provide an effective restraint on the exercise of market power:

...regulatory arrangements should be determined before the sale, to provide greater regulatory certainty to the purchaser. Governments must carefully consider the form of regulation that is appropriate. A price monitoring regime may be favoured by a government seeking to maximise the sale price. However, in the ACCC's experience, price monitoring does not provide an effective constraint on the exercise of market power, including monopoly power.⁹

5.11 The MUA argued that a leased Port of Darwin has the potential to produce an anti-competitive operating environment. It suggested that the NT Government's decision to lease the Port of Darwin to Landbridge amounted to a transfer of monopoly market power. The MUA maintained that the consequences of this decision are unlikely to be curtailed by a regulatory framework that is based on price monitoring.

National security and national interest considerations

5.12 In its submission to the committee, the Australian Strategic Policy Institute (ASPI) observed that Australia's foreign investment review framework is a multifaceted process that involves a number of discrete and complex steps. Many decisions will touch upon a range of interconnected issues, from national security to the implications of a proposed investment for Australia's competition policy. According to ASPI, the NT's decision to lease the Port of Darwin – and FIRB's response to that decision – highlighted a number of flaws in the review process.

5.13 ASPI maintained that the current framework privileges an expedited review process, whose primary aim is to facilitate a high degree of foreign direct investment. The unintended consequence of this 'structural' bias is to limit the critical attention that

7 Australian Consumer and Competition Commission, *Container Stevedoring Monitoring Report No. 16*, <https://www.accc.gov.au/system/files/ACCC%20stevedoring%20report%202014.pdf>, (accessed 9 December 2015).

8 Australian Consumer and Competition Commission, *Container Stevedoring Monitoring Report No. 16*, p. 21.

9 Australian Consumer and Competition Commission, *Container Stevedoring Monitoring Report No. 16*, p. 21.

is paid to the national security implications of some foreign investment proposals.¹⁰ As ASPI made clear in its submission:

Our view is that the current legislative and regulatory framework to manage foreign investment is inadequate in a number of respects. Current arrangements do not give sufficient consideration to the national security implications of foreign direct investment, especially as it relates to critical infrastructure.¹¹

5.14 According to ASPI, Australia's foreign investment review framework suffers from two interconnected problems. Firstly, the process for assessing foreign investment proposals is largely ad-hoc and lacks sufficient rigour and transparency. Secondly, this lack of procedural clarity brings with it the unintended consequence that governmental oversight, especially at its highest levels, including the National Security Committee of Cabinet, is at times inadequate in critical cases. ASPI maintained that national security concerns are the most likely to be overlooked as a result of a flawed assessment process, and this places the integrity of the review framework in doubt:

The processes for assessing investment proposals are ad-hoc, lack transparency and rigor and do not give government sufficient oversight in critical cases. As is very apparent from recent experience the result is that decisions to proceed – or not to proceed – with specific foreign investment requests are poorly explained to the public and give rise to confusion about how the government has exercised decision-making powers.¹²

5.15 Further, ASPI argued that the flaws in the process are the result of a number of gaps in FIRB's capacity to analyse the likely implications of foreign investment proposals. Among the more significant issues highlighted by ASPI are the following:

- The lack of a statutory basis for FIRB, which means that it cannot be separated from the Treasury, and is therefore, denied sufficient independence in its decision-making processes.
- The fact that FIRB only advises the Treasurer, and therefore does not report, through the Treasurer, to the National Security Committee of Cabinet.
- FIRB's secretariat appears to lack staff with the professional expertise required to make policy recommendations on national security matters.
- FIRB lacks a properly defined concept of critical infrastructure, which reveals a wider failing on the part of the Government.¹³

5.16 ASPI's criticisms of the current process for reviewing proposals for foreign investment, along with its suggested recommendations to address these shortcomings,

10 Australian Strategic Policy Institute, *Submission 4*, p. 2

11 Australian Strategic Policy Institute, *Submission 4*, p. 2.

12 Australian Strategic Policy Institute, *Submission 4*, pp. 2–3.

13 Australian Strategic Policy Institute, *Submission 4*, pp. 3–6.

focus on the need to ensure that FIRB does not neglect the national security component of the national interest equation.

5.17 In particular, given the fact that the Government's policy document explicitly defines an approach to assessment that avoids 'hard and fast rules'¹⁴ in favour of a case-by-case assessment, ASPI argued that the current review framework allows national security matters to be effectively sidelined. In part, this is because FIRB's secretariat does not appear to possess sufficient expertise in national security assessments to provide advice that considers more than the economic implications of a proposed investment. ASPI continued:

The current FIRB relies on Defence and the intelligence agencies to advise on the national security impacts of investment...The best way to deal with this situation is to strengthen the FIRB's internal capabilities to advise on national security matters. This will still require drawing on other departments to provide intelligence and other assessments, but it will at least make it possible for the FIRB to ask informed questions...To offer a sense of scale, a statutorily independent FIRB could function with a workforce of twenty to thirty APS staff, of which perhaps ten people might have professional expertise in traditional Treasury domains and ten be seconded from other agencies to work on defence, intelligence, critical infrastructure and national security assessments...¹⁵

5.18 According to ASPI, another primary fault of the current process is the fact that the concept of critical infrastructure is not a primary consideration in the assessment of proposals for investment.¹⁶ ASPI argued that the concept of critical infrastructure must be central to FIRB's advice to the Treasurer. According to Mr Peter Jennings, Executive Director of ASPI, in leasing the Port of Darwin Australia ceded effective strategic control over a major national security and critical infrastructure asset:

Australia's strategic interests, including responding to increasingly assertive Chinese maritime behaviour in the South and East China seas, now have to be balanced against the reality of operating out of a harbour run by a company whose website proclaims it is "contributing its best to ... realising the great rejuvenation of the Chinese dream". The Port of Darwin lease raises hard questions about the specifics of the deal and how Australian governments make sensible decisions on national security when considering foreign investment proposals.¹⁷

5.19 ASPI argued that, by ensuring that the concept of critical infrastructure is at the forefront of the review process, it is less likely that national security implications,

14 Treasurer, *Australia's Foreign Investment Policy*, December 2015, p. 1, http://firb.gov.au/files/2015/09/Australias_Foreign_Investment_Policy_December_2015_v2.pdf p. 1 (accessed 18 January 2016).

15 Australian Strategic Policy Institute, *Submission 4*, p. 4.

16 Australian Strategic Policy Institute, *Submission 4*, p. 6.

17 Peter Jennings, 'Darwin: Port in A Storm', *The Strategist*, 6 November 2015, <http://www.aspistrategist.org.au/darwin-storm-in-a-port/>, (accessed 9 December 2015).

as one component of the national interest equation, will be either overlooked or downplayed.¹⁸ The idea of critical infrastructure departs from the contention that infrastructure is little more than a purely physical asset, to which a straightforward monetary value can be assigned. As ASPI explained, the concept of critical infrastructure implies that some infrastructure assets are vital elements of Australia's national security framework:

From a strategic perspective the assessed dollar value of an element of critical infrastructure may not be the most relevant factor in considering the national security value of a potential foreign investment. There is, after all, only one Port of Darwin regardless of its commercial valuation. 'Infrastructure' shouldn't be thought of as only physical assets, but also production systems and networks. This includes such areas as maritime ports and airports, communications systems, power generation, distribution and transmission, hospitals and medical facilities, critical industrial capabilities used to support the Australian Defence Force, and essential Government infrastructure.¹⁹

5.20 ASPI further observed that, as the development and administration of the Government's critical infrastructure policy is the responsibility of the Attorney General's Department, it is important that strong ties between FIRB and the department are fostered and maintained.

5.21 Therefore, in order for these changes to occur and to incorporate national security concerns as an integral part of the evaluation of foreign direct investment, ASPI argued that the Government's framework for the assessment of foreign investment proposals must undergo further legislative, regulatory and administrative reform.

18 Australian Strategic Policy Institute, *Submission 4*, p. 7.

19 Australian Strategic Policy Institute, *Submission 4*, p. 7.