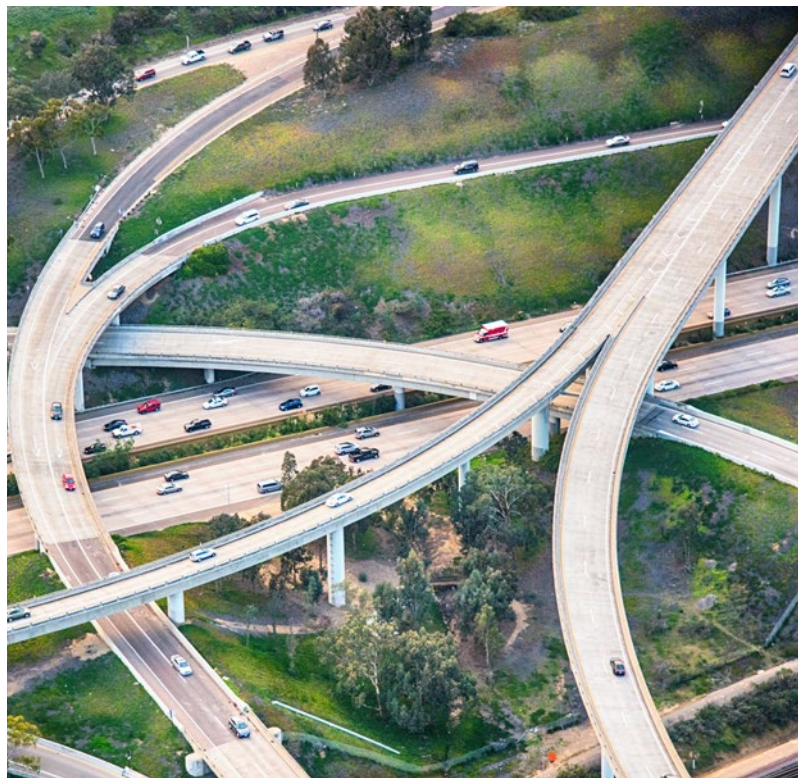
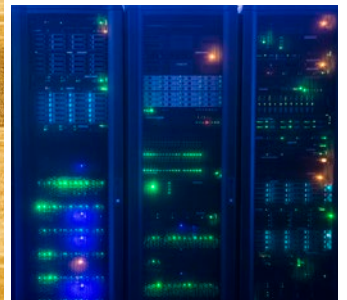
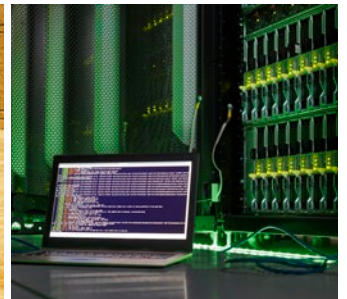
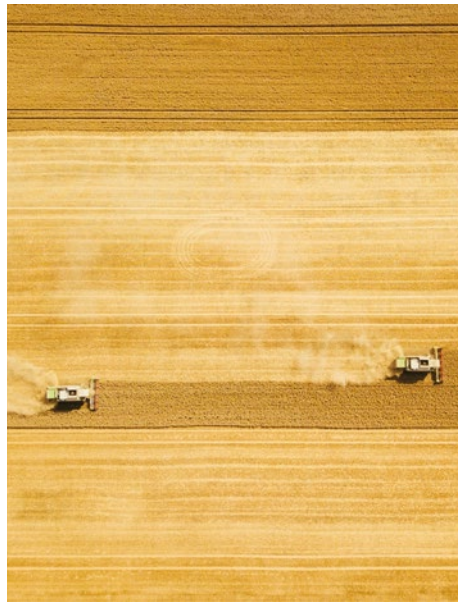




# AUSTRALIAN FOREIGN INVESTMENT REVIEW

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# Welcome

We are delighted to welcome you to the tenth edition of Herbert Smith Freehills' *Australian Foreign Investment Review*.

In this edition of the *Australian Foreign Investment Review*, we focus on the key takeaways from FIRB's 2017-18 Annual Report and new legislation relating to foreign investment, highlight some key issues for investors looking at data intensive sectors and the financial services sector and look forward to 2019.

Firstly, Malika Chandrasegaran and Daniel Chun provide a summary of the recent FIRB 2017-18 Annual Report, highlighting the key messages and themes. David Ryan and Bailee Walker review the history of CKI's bid for APA.

Philip Podzebenko and Jack McDonell consider the new Foreign Investment Transparency Scheme, which introduces new registration requirements for foreign investors with connections to a foreign government.

Natalie Bryce and Caitlin Walker review FIRB's approach to data privacy issues, which is of particular interest in healthcare and technology sectors. Tony Damian and Li-Lian Yeo look at the landscape for foreign investment in the financial sector, and the sector specific approvals required.

Finally, Matthew FitzGerald and Hayley Knaggs consider foreign investment in 2019, and the expected challenges for investors into Australia.

We trust you will enjoy the tenth edition of the *Australian Foreign Investment Review*.



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## About Herbert Smith Freehills

Herbert Smith Freehills has one of Asia Pacific's leading M&A legal practices, as well as the expertise and track record to help make any international investment in Australian assets a smooth and efficient process.

Our foreign investment experience includes navigating some of Australia's largest deals through the foreign investment review process.

We combine our transactional expertise with industry sector experience. We are acknowledged leaders in a number of global sectors including energy, mining and infrastructure, and technology, media and telecommunications.

# FIRB's Annual Report: Foreign investment trends and learnings

FIRB's Annual Report for the year ended 30 June 2018 was recently released. We discuss some key takeaways from the Report.



This article was written by

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## Overview

In February this year, FIRB released its annual report for the year ended 30 June 2018 (**Report**), providing data on the foreign investments applications considered during the year.

In summary, in respect of the 2017-2018 period, the Report shows:

- a 17.5% decrease in the value of approved foreign investment proposals;
- for the first time since 2012-2013, the United States surpassing China as the largest source of foreign investment approvals by value;
- the services sector and commercial real estate sector remain the top two sectors by value attracting foreign investment;
- a similar number of conditional approvals both by number and value when compared against the previous 2016-2017 period – the development of data security conditions in transactions that could involve sensitive data continued to be a key area of focus by FIRB;<sup>1</sup> and
- two rejections of foreign investment proposals, both relating to land acquisitions.

Treasury and the ATO have also stepped up their focus on enforcing compliance with the foreign investment rules. This included Treasury launching a pilot of its compliance audit program, with a total of 11 compliance audits conducted covering over \$25 billion in proposed investments. Following on from this pilot, Treasury has now established an annual audit program.

One interesting development over the course of the 2017-2018 period was the introduction on 1 July 2017 of a new business exemption certificate for the acquisition of interests in Australian assets or securities. It appears from the Report that 8 business exemption certificates were approved over the 2017-2018 period for total proposed investment up to \$3.1 billion. It will be interesting to see how this figure trends over the coming years.

FIRB has also signalled its continued focus on the assessment of sensitive assets across all dimensions of the national interest. This is against the backdrop of enhanced nationwide attention on sensitive assets, with the *Security of Critical Infrastructure Act 2018* (Cth) and the *Telecommunications Sector Security Reforms* having been introduced in 2018 to provide additional protections for critical

infrastructure and the telecommunications sector respectively in Australia.

We discuss these findings further below.

## Value and type of approvals generally

There were 11,145 foreign investment approvals in 2017-2018, representing approximately \$163.1 billion of proposed foreign investment. This represents a decline of 17.5% from the \$197.7 billion of approvals in 2016-2017, and a decrease of 34% from the \$247.9 billion of approvals in 2015-2016.

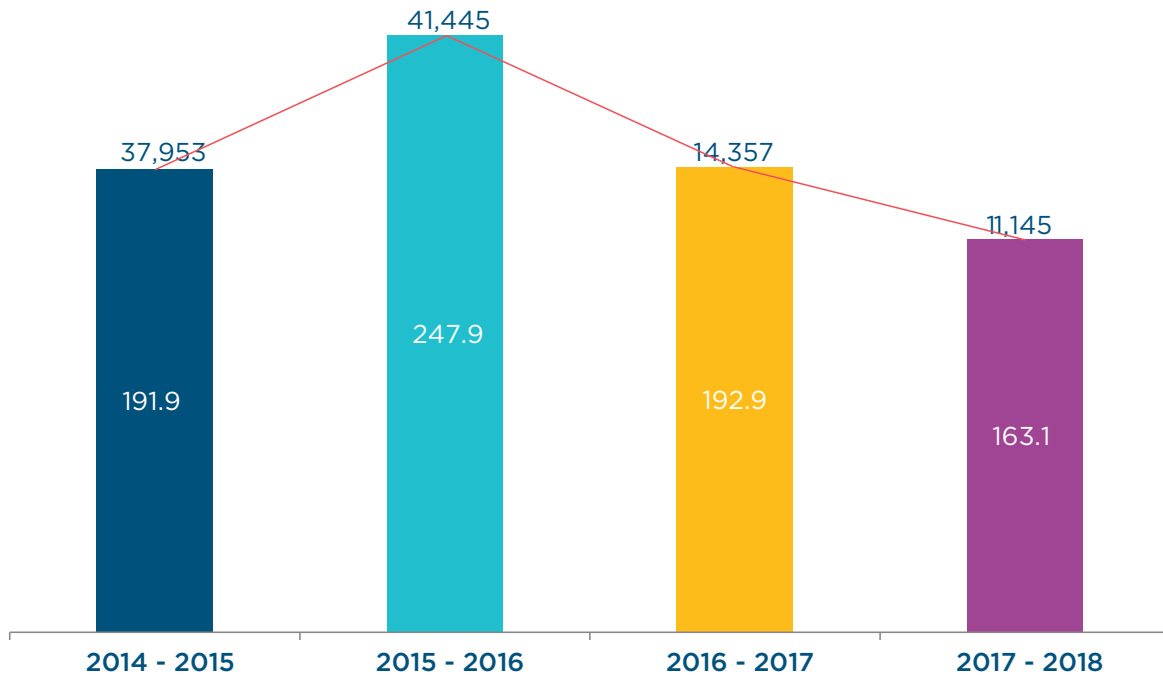
The Report, however, notes that the value of approvals in the three years prior to 2017-2018 were elevated in comparison to earlier years, for reasons including multiple competing approvals for high value targets in those years, and points to only two approvals of over \$2 billion in 2017-2018, compared to the 13 in 2016-2017 and 18 in 2015-2016.

There was a significant decline in certain sectors, including approvals in the:

- manufacturing, electricity and gas sector declining to \$16.6 billion in 2017-2018, a 59% decrease from the \$40.9 billion of approvals in 2016-2017; and

1. See N Bryce and C Walker "Foreign investment in data intensive sectors: FIRB's role in protecting Australia's data".

## Total value (A\$b) and number of foreign investment approvals



Source: FIRB Annual Reports 2014-2015, 2015-2016, 2016-2017 and 2017-2018.

- commercial real estate sector totalling 391 in number with a total value of \$39.5 billion (down from the 465 approvals totalling \$43.7 billion in 2016-2017).

The reason for the decline in the manufacturing, electricity and gas sector partly reflects the high value of approvals in 2015-2016 and 2016-2017 that was driven by the sale of parts of the NSW Government's electricity transmission networks.

Foreign investment approvals in certain sectors, however, increased from their 2016-2017 levels, with approvals in the:

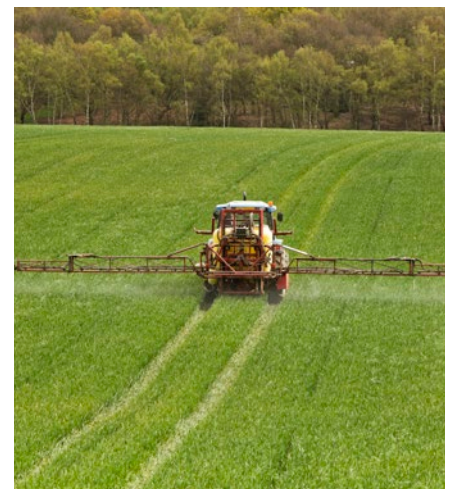
- services sector totalling \$63.2 billion, a 17% increase from 2016-2017 – however, over 40% of the total value of approvals in this sector can be attributed to the approval for the Unibail-Rodamco merger with Westfield for a proposed investment value of \$28 billion;
- agriculture, forestry and fishing sector of \$7.9 billion (an increase of \$0.9 billion);
- finance and insurance sector of \$6 billion (an increase of \$2.2 billion); and
- minerals and exploration sector of \$17.4 billion (an increase of \$1.5 billion).

### Sources of foreign investment

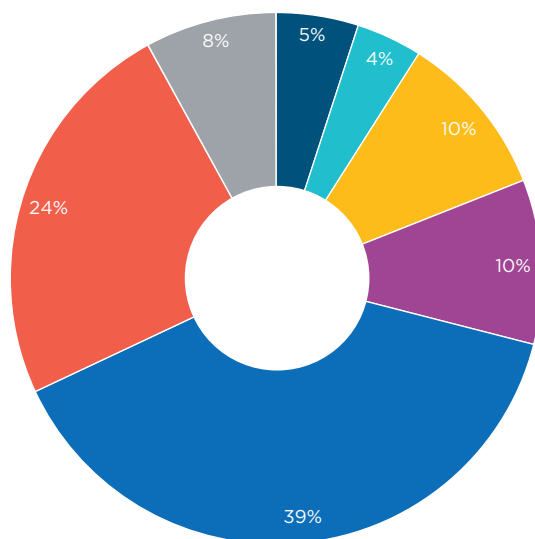
For the first time since 2012-2013, the United States replaced China as the largest overall source of approved foreign investment by value (\$36.5 billion). United States' approvals in 2017-2018 was \$36.5 billion, a 38% increase from the \$26.5 billion in approvals in 2016-2017, with notable increases in proposed investment in the services sector and the manufacturing, electricity and gas sector.

With respect to China, there was a 30% decline in the number of approvals, and almost a 40% fall in the value of these approvals, with \$23.7 billion of approvals in 2017-2018 compared to the \$38.9 billion in approvals in 2016-2017. There was a notable decrease in the manufacturing, electricity and gas sector, the mineral exploration and development sector, the services sector, and in real estate for Chinese proposed investment.

However, the Report points out that the International Monetary Fund and Australian Bureau of Statistics data to the end of 2017 indicate an overall decrease in Chinese outward investment, and that Australia has been impacted to a smaller degree compared to similar economies.



## Total value of foreign investment approvals by sector



Source: FIRB Annual Report 2017-2018.

China was followed by the United Kingdom (\$17.7 billion), Singapore (\$11.3 billion), Canada (\$11 billion), Netherlands (\$10.4 billion) and France (\$9.9 billion). These figures represent a substantial increase in approvals for the United Kingdom, Netherlands and France compared to the previous 2016-2017 period, with approvals for the United Kingdom up \$13.6 billion, Netherlands up \$6.3 billion and France also greatly increased.

Netherlands' and France's high level of investment in 2017-2018 is largely attributable to the merger between Unibail-Rodamco (dual listed on French and Dutch stock exchanges) and Westfield – previously Netherlands was ranked no. 9 in 2016-2017 for approvals value and France was ranked outside the top 18 countries. The merger also increased the approvals value for the United Kingdom due to the shareholders located there.

### Rejections and conditional approvals

Two applications were rejected in 2017-2018 compared to the three rejections in 2016-2017. One of these was in the residential real estate sector, and the

other related to a proposed acquisition of agricultural land for the purpose of residential development.<sup>2</sup>

Three applications for an exemption certificate were declined by the Treasurer – it is unclear what type of exemption certificates these were.

Conditions were applied to approximately 43% of the total number of applications and over 75% of the total value of approvals, representing similar levels to 2016-2017 where conditions applied to approximately 40% of the total number of applications and 70% of the total value. For proposed investments outside real estate, the majority of the conditions were tax related. That said, FIRB has flagged that given the growing interest in health and financial services businesses, as well as significant foreign interest in critical infrastructure and data centres, the development of data security conditions continued to be a key area of focus for FIRB which they have indicated is to ensure that a change of ownership does not present an unmanaged risk of unauthorised access to personal, government or sensitive operational data.

### Stepped up focus on compliance and enforcement

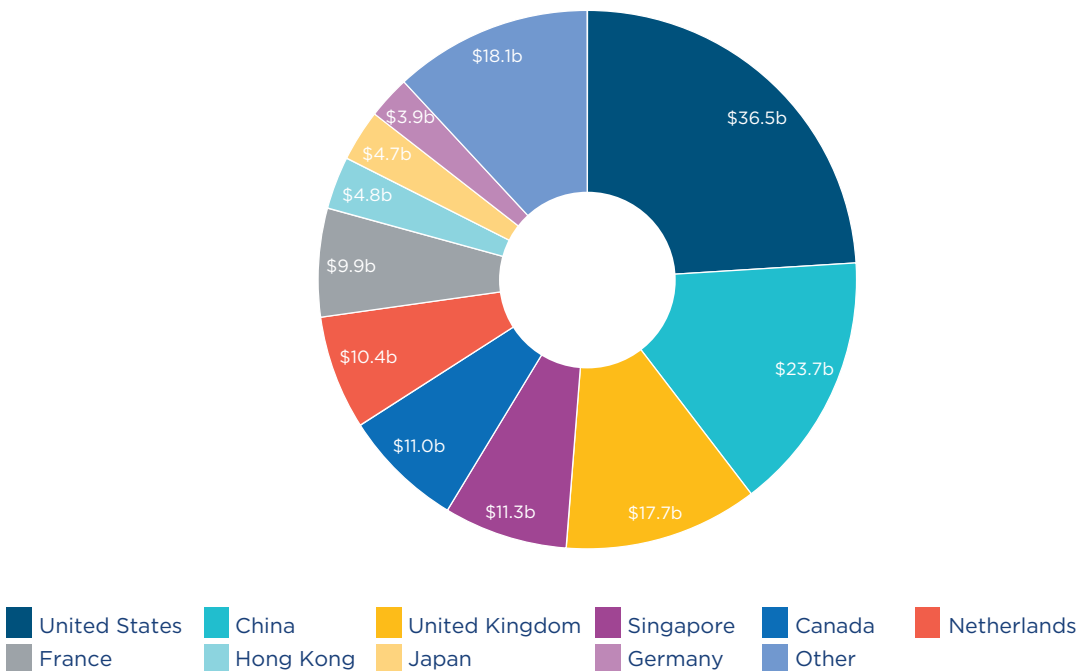
Compliance and enforcement has been a clear focus of both the Treasury and the ATO in recent years, and has been a key agenda item also in 2017-2018. The ATO took on responsibility for managing residential real estate applications and associated compliance work in 2015, and since April 2017 has assumed additional responsibility for screening applications and for compliance work for non-sensitive commercial real estate and corporate reorganisations.

Since September 2017 when Treasury announced its increased focus on enhancing its compliance arrangements for foreign investments, Treasury has developed a compliance assurance program which includes compliance audits.

A pilot of the compliance audit program was completed in 2017-2018, with a total of 11 compliance audits conducted covering over \$25 billion in proposed investments, and Treasury has now established an annual audit program. FIRB has noted that these activities have revealed that foreign investors are largely meeting obligations and have not revealed compliance issues warranting enforcement action.

2. Post June 2018, Treasury also rejected the proposed \$13 billion takeover of APA Group by Hong Kong listed CK Infrastructure Group. See D Ryan and B Walker "Case study: FIRB's Rejection of Proposed Takeover of APA Group by CKI".

**Sources of foreign investment in 2017-2018 by country**



Source: FIRB Annual Report 2017-2018.

**Developments in FIRB’s assessment of national interest**

The Report also notes that FIRB has continued its focus on ensuring sensitive assets are thoroughly assessed across all dimensions of the national interest with FIRB seeking to provide early guidance to potential investors where possible. This is against the backdrop of the introduction of the Critical Infrastructure Centre in January 2017 and enhanced nationwide attention on sensitive assets, with the *Security of Critical Infrastructure Act 2018* (Cth) and the *Telecommunications Sector Security Reforms* having been introduced in 2018 to provide additional protections for critical infrastructure and the telecommunications sector respectively in Australia.

FIRB has also flagged that it is also closely examining foreign investment developments overseas, and the significant reforms being made to foreign investment regimes in relation to national security issues in the United States, the United Kingdom and other countries. The Report stresses that FIRB will continue to scrutinise ways to strengthen its review procedures, including by drawing upon the practices of other countries where they can be learned from.

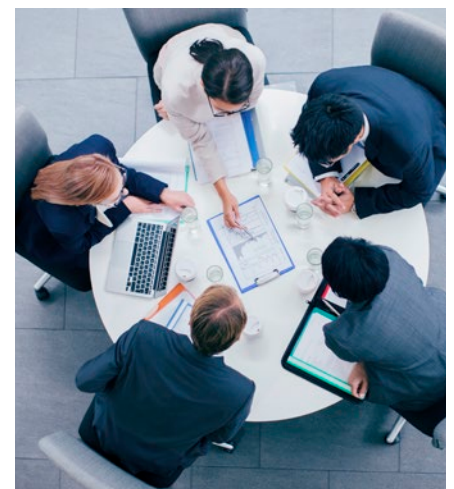
**Conclusion and key takeaways for investors**

The Report has provided useful insights into the trend of foreign investments flowing into Australia. Key takeaways for foreign investors who require FIRB approval are:

- engage with FIRB early, particularly where the proposed acquisition is of a sensitive asset or critical infrastructure;
- where the proposed target deals with sensitive or personal data, be prepared for the potential inclusion of data security conditions; and
- to put in place systems to ensure ongoing compliance with conditions imposed by FIRB.

**More information**

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# Case study: FIRB's Rejection of Proposed Takeover of APA Group by CKI



## This article was written by

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## Introduction

In November 2018 the Federal Treasurer, the Hon. Josh Frydenberg, rejected the proposed takeover of the ASX-listed APA Group (APA) by a consortium led by CK Infrastructure Holdings Limited (CKI).

This briefing examines the Treasurer's decision and its broader implications for the foreign investment review process in Australia.

## Background

APA is a leading Australian energy infrastructure business and the largest

owner of gas transmission assets in Australia.<sup>3</sup> It operates a portfolio of assets in excess of A\$20 billion,<sup>4</sup> which includes 56% of Australia's total gas transmission assets, 74% of the gas transmission assets in New South Wales and Victoria and 64% of the gas transmission assets in the Northern Territory.<sup>5</sup>

In June 2018 an indicative, non-binding proposal to acquire all of the stapled securities in APA was made by CKI,<sup>6</sup> a global infrastructure company listed on the Hong Kong Stock Exchange. Founded by prominent Hong Kong businessman Li Ka Shing, CKI has a diversified portfolio of

infrastructure assets in more than 50 nations,<sup>7</sup> including Australia, New Zealand, the United Kingdom, Germany, Canada, Hong Kong and mainland China.<sup>8</sup>

In August 2018 the proposed acquisition, worth approximately A\$13 billion,<sup>9</sup> was formalised by the execution of an Implementation Agreement by the parties.<sup>10</sup> The Implementation Agreement was subject to a number of conditions, including approval of the transaction by:

- the Treasurer under the *Foreign Acquisitions and Takeovers Act 1975* (Cth);<sup>11</sup> and

3. Australian Financial Review, *CKI's bid for APA Group officially rejected by Treasurer Josh Frydenberg*, 21 November 2018, <https://www.afr.com/news/policy/foreign-investment/ckis-bid-for-apa-group-officially-rejected-by-treasurer-josh-frydenberg-20181120-h1850d>.
4. APA Group Website, *About APA*, <https://www.apa.com.au/about-apa/>.
5. The Hon Josh Frydenberg Media Release, *Proposed acquisition of APA*, 7 November 2018, <http://jaf.ministers.treasury.gov.au/media-release/046-2018/>.
6. APA ASX Announcement, *APA Grants Due Diligence in Response to Receipt of an Indicative Non-Binding Proposal from CKI*, 13 June 2018, <https://www.apa.com.au/news/asx-releases/2018/apa-grants-due-diligence-in-response-to-receipt-of-an-indicative-non-binding-proposal-from-cki/>.
7. Sydney Morning Herald, *China fears on \$13b gas deal 'naïve, ill-informed'*, 21 September 2018, <https://www.smh.com.au/business/companies/china-fears-on-13b-gas-deal-naive-ill-informed-20180919-p504ts.html>.
8. CKI, *CKI at a Glance*, accessed 25 March 2019, [https://www.cki.com.hk/english/about\\_CKI/cki\\_at\\_a\\_glance/index.htm](https://www.cki.com.hk/english/about_CKI/cki_at_a_glance/index.htm).
9. Australian Financial Review, *CKI bidding for APA Group in \$13b deal*, June 13 2018, <https://www.afr.com/street-talk/cki-bidding-for-apa-group-in-13b-deal-20180613-h11b10>.
10. APA ASX Announcement, *APA and CKI Consortium Enter Into Implementation Agreement*, 13 August 2018, <https://www.apa.com.au/news/asx-releases/2018/apa-and-cki-consortium-enter-into-implementation/>.
11. Implementation Agreement, clause 3.1(a).



- the Australian Competition and Consumer Commission (**ACCC**) under the *Competition and Consumer Act 2010* (Cth) (**Competition and Consumer Act**).<sup>12</sup>

### ACCC Decision

On 12 September 2018 the ACCC announced that it would not oppose the CKI acquisition of APA. The decision was made following the acceptance of a court-enforceable undertaking by CKI to divest significant gas assets in Western Australia following completion of the transaction.

While the ACCC expressed concern that the proposed transaction would

substantially lessen competition in relation to new pipeline development and gas transmission and storage services in Western Australia, it found that these concerns could be adequately addressed by the CKI undertaking.<sup>13</sup>

### FIRB Decision

An initial application by CKI to the Foreign Investment Review Board (**FIRB**) in respect of the proposed acquisition was made in August 2018.<sup>14</sup>

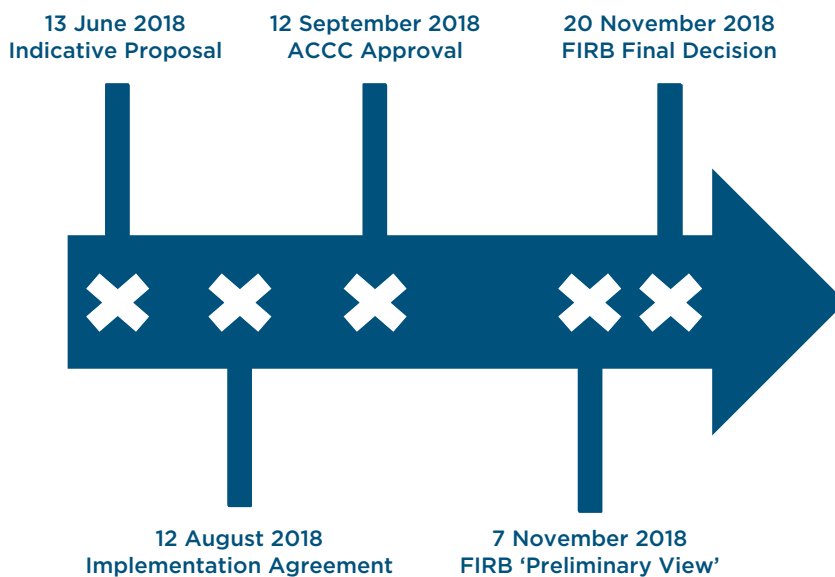
On 7 November 2018 the Treasurer announced a 'preliminary view' that CKI's acquisition of APA would be contrary to the national interest. The Treasurer's decision

was made on the grounds that the transaction would result in 'undue concentration of foreign ownership by a single company group in our most significant gas transmission business'.<sup>15</sup>

While announcement of the Treasurer's 'preliminary view' gave rise to speculation that the deal could be restructured to address the concerns raised, CKI did not revise its bid.<sup>16</sup> On 20 November 2018 the Treasurer made a final decision to reject the acquisition for the same reasons expressed in his 'preliminary view'.<sup>17</sup>

### Timeline

A timeline of the proposed acquisition and the ACCC and FIRB approval processes is set out below.



12. Implementation Agreement, clause 3.1(c).

13. ACCC Media Release, ACCC will not oppose acquisition of APA, 12 September 2018, <https://www.accc.gov.au/media-release/accc-will-not-oppose-acquisition-of-apa>.

14. Australian Financial Review, *FIRB decision on CKI-APA deal extended for another 90 days*, 24 October 2018, <https://www.afr.com/business/firb-decision-on-ckiapa-deal-extended-for-another-90-days-20181024-h171x8>.

15. See footnote 10.

16. Sydney Morning Herald, *Revised CKI bid for APA may get green light after knockback*, 9 November 2018, <https://www.smh.com.au/politics/federal/revised-cki-bid-for-apa-may-get-green-light-after-knockback-20181108-p50ete.html>.

17. The Hon Josh Frydenberg Media Release, *Final decision on the proposed acquisition of APA*, 20 November 2018, <http://jaf.ministers.treasury.gov.au/media-release/055-2018/>.

## Aspects of interest

- CKI is already a significant investor in Australian gas and electricity infrastructure. CKI's existing investments in Australia include interests in electricity distribution businesses SA Power Networks, Powercor, Citipower and United Energy; gas distribution businesses Australian Gas Networks Limited and Multinet Gas; and the Dampier Bunbury pipeline (a gas pipeline connecting the Canarvon / Browse Basin to Perth).
- This is not the first time that a proposal by CKI to invest in Australia has been rejected by the Treasurer. In August 2016 the then-Treasurer, the Hon. Scott Morrison, rejected proposals from CKI and rival bidder State Grid (a state-owned Chinese corporation) to acquire a 50.4% interest in a 99 year lease of Ausgrid, the operator of the largest electricity distribution network in New South Wales.<sup>18</sup>
- The APA decision can be distinguished from the Ausgrid decision, which was expressly made on the grounds of national security. Although the specific reasons for the Ausgrid decision have never been publically disclosed, it is understood that the Ausgrid business presented some specific and unique national security concerns (including the fact that Ausgrid hosts a piece of infrastructure that is a critical support to the Pine Gap intelligence facility near Alice Springs).<sup>19</sup> Despite public speculation about the national security

implications of the APA acquisition (discussed further below), the Treasurer's decision was ultimately based on concerns about market concentration and does not expressly refer to issues of national security.

- The Treasurer's announcements focused on the aggregation of interests in the gas transmission sector, notwithstanding that the ACCC had already determined that the transaction (when accompanied with an enforceable undertaking regarding divestments) did not result in a substantial lessening of competition.
- This difference in outcome highlights that the 'national interest' factors considered by FIRB in advising the Treasurer include the impact on competition in Australia, and that the competition aspects considered by FIRB are potentially broader than competition aspects considered by the ACCC under the Competition and Consumer Act.
- Under section 50 of the Competition and Consumer Act, the test to be applied by the ACCC in determining whether to oppose a transaction is whether the transaction would have the effect, or be likely to have the effect, of substantially lessening competition in any market. The ACCC does not have the power to intervene in the acquisition of an entity that already has significant market power unless the transaction will result in a further substantial lessening of competition. In a media release relating its decision, the ACCC noted that most concerns about the acquisition that were

raised by industry participants related to APA Group's pre-existing dominance in gas transmission.<sup>20</sup> While these concerns were beyond the scope of the ACCC's review, it appears that they were relevant to FIRB's assessment of whether the acquisition was therefore in the national interest.

- There were a number of vocal opponents to the APA acquisition. In the months leading up to the Treasurer's decision a number of politicians (such as Liberal backbencher Jim Molan and cross bench senators Pauline Hanson and Rex Patrick) called for the deal to be blocked. Interestingly, the bulk of the opposition to the deal was based on perceived national security risks arising from ownership of the APA gas network by a 'Chinese' company.<sup>21</sup> As highlighted above, these reasons were not cited by the Treasurer in his preliminary or final decision.
- There is an increasing focus on foreign ownership of Australian infrastructure. In the three year period from January 2016 to December 2018 FIRB has made as many refusals of business investments as it did in the 15 year period from January 2000 to December 2015.<sup>22</sup> The three refusals made in the 2000-2015 period were the rejections of Royal Dutch Shell's proposed acquisition of Woodside Petroleum in 2001,<sup>23</sup> of the Singapore Exchange's proposed acquisition of the Australian Securities Exchange in 2011<sup>24</sup> and of Archer Daniels Midland proposed acquisition of Graincorp in 2013.<sup>25</sup> The three refusals in the 2016-2018 period

18. The Hon. Scott Morrison Media Release, *Foreign investment applications for the 99-year lease of Ausgrid*, 11 August 2016, <http://sjm.ministers.treasury.gov.au/media-release/067-2016/> and The Hon. Scott Morrison Media Release, *Statement on decision to prohibit the 99-year lease of 50.4 per cent of Ausgrid under current proposed structure*, 19 August 2018, <http://sjm.ministers.treasury.gov.au/media-release/069-2016/>.

19. Sydney Morning Herald, *Revealed: Why the sale of Ausgrid to Chinese buyers was vetoed*, 28 May 2018, <https://www.smh.com.au/opinion/revealed-why-the-sale-of-ausgrid-to-chinese-buyers-was-vetoed-20180528-p4zhxh.html>.

20. See footnote 14.

21. See for example Australian Financial Review, *CKI pipeline bid risks veto on national security grounds*, 12 September 2018, <https://www.afr.com/news/politics/cki-pipeline-bid-risks-veto-on-national-security-grounds-20180912-h159ar>, Sydney Morning Herald, *China fears on \$13b gas deal 'naive, ill-informed'*, 21 September 2018, <https://www.smh.com.au/business/companies/china-fears-on-13b-gas-deal-naive-ill-informed-20180919-p504ts.html>, Sydney Morning Herald, *CKI bid: FIRB has learnt lessons from Port of Darwin sale: senator*, 24 October 2018, <https://www.smh.com.au/business/the-economy/cki-bid-firb-has-learnt-lessons-from-port-of-darwin-sale-senator-20181024-p50bp2.html>.

22. ABC News, *Rare FIRB speech reveals review process at odds with public sentiment around foreign investment in farmland*, 22 June 2017, <https://www.abc.net.au/news/rural/rural-news/2017-06-22/firb-review-at-odds-with-public-sentiment/8639754>.

23. The Hon. Peter Costello Media Release, *Foreign Investment Proposal - Shell Australia Investments Limiteds (Shell) Acquisition Of Woodside Petroleum Limited (Woodside)*, 23 April 2001, <http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2001/025.htm&pageID=003&min=phc&Year=2001&DocType=0>.

24. The Hon. Wayne Swann Media Release, *Foreign Investment Decision*, 8 April 2011, <http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2011/030.htm&pageID=003&min=wms&Year=2011&DocType=0>.

25. The Hon. Joe Hockey Media Release, *Foreign investment application: Archer Daniels Midland Company's proposed acquisition of GrainCorp Limited*, 29 November 2013, <http://jhb.ministers.treasury.gov.au/media-release/026-2013/>.

were the rejection of CKI and State Grid on the sale of Ausgrid, of Dakang on the proposed acquisition of S. Kidman and Co. Limited and of CKI on the proposed acquisition of APA.<sup>26</sup>

- The Treasurer's announcement noted that his decision had been reached in close consultation with both FIRB (which was not able to come to a unanimous recommendation) and the Critical Infrastructure Centre (CIC),<sup>27</sup> an organisation established in January 2017 to safeguard Australia's critical infrastructure (which includes critical gas infrastructure) from national security risks.<sup>28</sup> This provides an insight into the decision making process and highlights the Treasurer's ultimate discretion in relation to foreign investment applications.

### Key lessons learned

- While FIRB and the Treasurer continue to stress that Australia welcomes foreign investment,<sup>29</sup> foreign investors considering the purchase of critical infrastructure should be aware that their proposals will be subject to greater scrutiny than in previous years, including at a political level.
- In particular, foreign investors should take the involvement of the CIC into consideration in relation to the overall timeline of the approval process, engage with FIRB early and address potential concerns in their application.
- The stated reason for rejection of the APA transaction was the level of

concentration of foreign ownership that would have resulted from the deal. This was in part due to APA's pre-existing market dominance. Foreign investors should note that competition considerations form part of the 'national interest' test applied by FIRB and that the matters considered by FIRB will be broader than the matters considered by the ACCC.

- Where a potential acquisition gives rise to concerns about market aggregation, foreign investors should consider whether those concerns could be addressed through structuring. Structuring options available include partnering with an Australian company, taking a cornerstone or majority stake in an ASX-listed company (and keeping public shareholders on the register) or undertaking to divest certain assets.

### More information

For more information, please contact David Ryan at [david.ryan@hsf.com](mailto:david.ryan@hsf.com)

26. The Hon. Scott Morrison Media Release, *Preliminary decision of foreign investment application for purchase of S. Kidman & Co Limited*. We note that the sale of S. Kidman and Co Limited was subsequently approved by the Treasurer in December of 2017 following a restructure of the deal that saw an Australian entity take a majority interest. See further: The Hon. Scott Morrison Media Release, *Approval of S. Kidman & Co. Limited sale to increase Australian ownership*, 9 December 2017, <http://sjm.ministers.treasury.gov.au/media-release/130-2016/>.

27. See footnote 10.

28. Herbert Smith Freehills, *Australian Government to heighten controls over critical electricity, port and water infrastructure assets*, 16 October 2017, <https://www.herbertsmithfreehills.com/uk/grads/latest-thinking/australian-government-to-heighten-controls-over-critical-electricity-port-and-water> and Herbert Smith Freehills, *The new Critical Infrastructure Centre and Implications for the Foreign Investment Approval Process*, 29 June 2018, <https://www.herbertsmithfreehills.com/latest-thinking/the-new-critical-infrastructure-centre-and-implications-for-the-foreign-investment>.

29. See footnotes 10 and 17 and *Australia's Foreign Investment Policy*, [https://cdn.tspace.gov.au/uploads/sites/82/2018/12/1-January-2019-Policy\\_.pdf](https://cdn.tspace.gov.au/uploads/sites/82/2018/12/1-January-2019-Policy_.pdf).

# Foreign Influence Transparency Scheme: What is it and will you need to register?

A new scheme operating through the Attorney-General's Department of the Australian government passed through Parliament on 10 December 2018, with the grace period for registration ending on 10 March 2019, persons operating in Australia with foreign government ownership or control may need to self-register for the scheme to avoid penalties.



## This article was written by

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## Background

Following the passage of the *Foreign Influence Transparency Scheme Act 2018* (Cth) (**FITS Act**) through Parliament on 10 December 2018, persons (including entities) that undertake prescribed activities on behalf of foreign principals are now required to self-register for the Foreign Influence Transparency Scheme (**Scheme**).

## Who needs to register under the Scheme?

Although the focus of the FITS Act appears to be foreign government entities actively involved in political lobbying, the FITS Act potentially applies to a broader range of persons and activities.

A person must register under the Scheme if they undertake a **registrable activity** on behalf of a **foreign principal**.

## What are registrable activities?

The following activities have the potential to be registrable if the sole, primary or substantial purpose of the activity is political or governmental influence:

- **Parliamentary lobbying** – lobbying a Member of Parliament or their staff;
- **General political lobbying** – lobbying a Commonwealth official, Commonwealth authority, registered political party,

candidate in a federal election or registered political campaigner;

- **Communications activity** – communicating or distributing information or material to the public; or
- **Disbursement activity** – distributing money or other things of value where disclosure is not already required.

Persons who undertake any of the above activities for the purpose of political or governmental influence, will need to assess whether their actions are being performed for or on behalf of a foreign principal.

If the party performing the actions is itself a foreign government undertaking political lobbying, it is not necessary to show that the actions are undertaken for the purpose of political or governmental influence for the activity to be registrable.

## Who will be deemed to be foreign principals?

There are four types of foreign principals under the FITS Act:

- foreign governments;
- foreign political organisations;
- foreign government related entities; and
- foreign government related individuals.

The FITS Act defines 'foreign government' to include 'an authority of the government of a foreign country'. At this stage guidance has not been published clarifying if state-owned enterprises and sovereign wealth funds will be treated as foreign governments for the purposes of the FITS Act.

An entity will be a foreign government related entity if:

- a foreign government has a 15% ownership or voting stake in the company, or the ability to appoint 20% of the company's directors (**Ownership Tests**); or
- its directors are accustomed to acting as directed by a foreign government, or a foreign government otherwise exercises substantial control over it (**Control Tests**).

## How and by when must a person register?

The Attorney-General's Department has put in place a registration portal to assist persons to determine whether or not they are required to register or if the person is able to rely on an exemption to registration (including for industry representative bodies, registered charities and other select groups).

After the initial grace period ends on 10 March 2019, a person must apply for registration under the Scheme within



14 days of undertaking any registrable activities to avoid penalties.

### Do registrants have any ongoing obligations?

Registrants are subject to a range of requirements including annually renewing registration, confirming and updating details on the register when registrable activities occur and keeping records for up to three years after registration ends.

A number of requirements under the scheme are triggered as Commonwealth election periods approach. Registered persons will need to ensure that procedures have been put in place to ensure continued compliance with these increased reporting obligations.

### What information is publicly available on the register?

The public register accessible at <https://transparency.ag.gov.au/> contains details of the registrant, the foreign principal and the activities and arrangements which are being undertaken with the foreign principal.

Under the FITS Act, information must not be included on the transparency register if it is commercially sensitive or affects national security. Despite this, the responsibility to assert that information is commercially sensitive rests with the party providing the information and it is not yet

clear what information will be deemed to be commercially sensitive.

### What powers does the Government have in relation to the Scheme?

The FITS Act contains broad powers for the secretary administering the Scheme to issue a provisional transparency notice to a person it is satisfied is a foreign government related individual or entity.

A person has 14 days to make submissions after being issued with a transparency notice. Each transparency notice issued by the secretary will be made public, however the FITS Act does not state that any responses will be made public.

Once the provisional notice is issued, the person is taken to be a foreign government related individual or entity under the FITS Act.

### More information

For more information, please contact Philip Podzebenko at [philip.podzebenko@hsf.com](mailto:philip.podzebenko@hsf.com)



# Foreign investment in data intensive sectors: FIRB's role in protecting Australia's data

The Foreign Investment Review Board is increasingly focused on protecting Australia's data. We take a look at the steps that are being taken, particularly in the context of healthcare and technology M&A.



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## Introduction

While the past two years have seen a lot of discussion about how best to manage the use, sharing and protection of Australian's personal data, the government is yet to produce a clear policy governing the approach to privacy and data security. In the absence of such a clear mandate, FIRB has developed its own policies in this area, and is increasingly uniting data security with national security.

In 2018, David Irvine AO, Chair of FIRB, speaking to the International CEO Forum, noted the Critical Infrastructure Centre's (CIC) role in helping to provide a more comprehensive approach to managing national security risks to critical infrastructure, the increasing use of conditions to manage identified national security risks and also that:

*"Security of data is a growing area of sensitivity. The Government has an obligation to promote the protection of the private or personal data of Australian citizens. How and where it is stored and who has access to it."*

This focus on data protection has been felt most keenly in the areas of healthcare and technology M&A, two data intensive sectors with strong M&A activity. In its most recent annual report, FIRB noted the increasing complexity presented by privatisation of

large state-owned electricity assets and the sales of data centres in a heightened national security environment, and the significant foreign interest in critical infrastructure assets and data centres and increasingly in large health and financial services businesses (such as Permira's acquisition of the I-MED Radiology Network, which it specifically called out as raising data security concerns that warranted conditions being imposed).

## Data Protection and National Security

In evaluating takeovers of Australian businesses by foreign companies, FIRB has a broad mandate to protect Australia's national security interests through the imposition of conditions, or to block investment entirely.

In 2017, this mandate was strengthened with the creation of the CIC, which was established to safeguard Australia's critical infrastructure from national security risks such as sabotage, espionage and coercion. FIRB consults with the CIC on applications for foreign investment which relate to "critical infrastructure".

At present, "critical infrastructure" is defined under the *Security of Critical Infrastructure Act 2018* (Cth) as being certain electricity assets, gas assets, ports and water assets but the Act also allows for assets to be declared through the processes

under the Act or prescribed by the Rules as critical infrastructure.

The CIC also has a role in respect of telecommunications infrastructure, which was considered to be the highest-risk critical infrastructure sector and was subject to separate legislative reform.

While data sensitive assets and the healthcare and technology sectors have not yet risen to the level of "critical assets", it is clear that investment in these areas is being considered in tandem with national security concerns, as generally, both FIRB and the CIC are alive to the risks posed to national security from technological changes and the threat of cyber-attack. For example, the risk assessments conducted by the CIC involve collecting information on data holdings and information technology systems of the business or those necessary for the operation of the asset, and on interdependencies with other priorities (particularly in relation to water assets, hospitals and health centres have been noted as key interdependent assets).

## FIRB's approach

Despite the strong association between concerns of national security and concerns of data protection, to date this has been addressed through internal FIRB policy and not through legislative change. For example,

a data intensive business is not considered as a "sensitive business", unless the business also falls under the existing limbs of the definition (businesses carried on in the media or telecommunications sectors, and business relating to the development, manufacture or supply of, or the provision of services relating to, encryption and security technologies and communications systems being the most directly relevant limbs). Therefore, for a foreign investor from an "agreement country" the higher threshold of \$1,154 million must still be met before the acquisition is a significant action or notifiable action under the Act.

However, in some circumstances, there may be uncertainty as to whether a business will be a "sensitive business" or whether a foreign investor is a "foreign government investor", given the broad drafting of the legislation. In those cases, some investors are choosing to voluntarily notify FIRB of a proposed acquisition.

While this strategy allows FIRB to consider a transaction it may otherwise not have looked at, it has the benefits of front-ending the FIRB review process, avoiding delays to the completion timetable, and eliminating the risk that FIRB could request that a transaction be unwound. This strategy is particularly relevant for data-intensive sectors, where investors are on notice that FIRB is interested.

### Data Protection Conditions

Where FIRB has been notified of a transaction in a data-intensive sector, or otherwise has jurisdiction to review the

transaction, FIRB's stated preference is to impose conditions on the transaction in relation to data protection, and not to block all foreign investment. In developing the conditions to be imposed on a transaction, FIRB will consider the type of data in question (while health data is a clear focus, FIRB is concerned with the security of Australian's personal data more generally as well as the use of government data and sensitive operational data), where that data is stored and how it is accessed.

Unlike in relation to tax compliance, to date, standard conditions in relation to data protection have not been published. While the conditions will depend on FIRB's assessment of the business, recent experience suggests foreign investors in data-intensive businesses, or businesses with access to sensitive data could expect conditions to be imposed:

- preventing sensitive data from leaving Australia, or requiring companies to notify customers if information is stored overseas;
- preventing shareholders, the board or other members of the corporate group from accessing sensitive data, particularly at a customer level;
- requiring companies to appoint a specific individual with responsibility for the data to be responsible for compliance and reporting breaches to FIRB; and
- requiring ongoing monitoring and reporting to both FIRB and individual customers as relevant.

Such conditions should not prevent investors from operating the business in Australia, or launching the same technology overseas but they are likely to add operational complexity, particularly for investors managing otherwise integrated corporate groups.

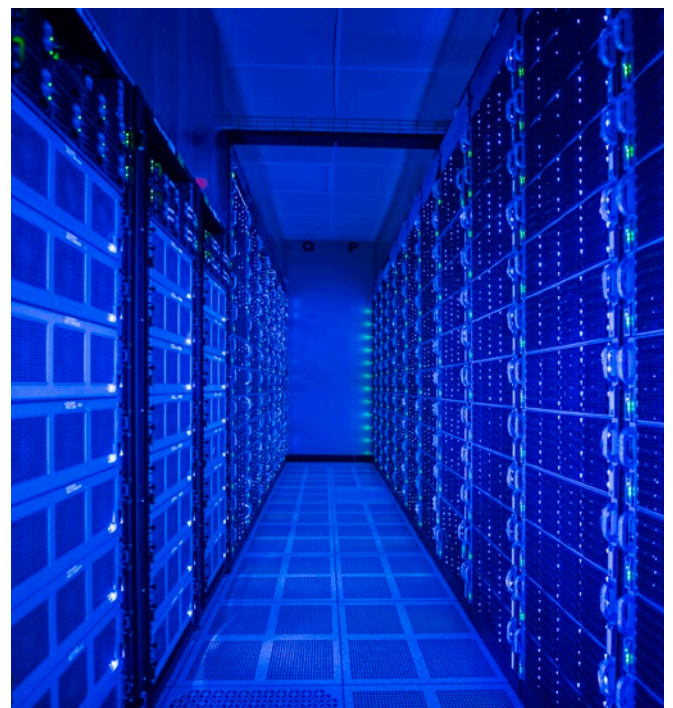
### Conclusions and commentary

Data security is likely to remain a key issue for FIRB, the CIC and the Australian government generally, particularly where foreign investment is concerned. Going forward, this focus on data security and national security may lead to FIRB and the CIC working together to take a stronger role in the protection of Australian data.

Investors should be on notice that FIRB will focus on data storage and access wherever personal information is concerned, regardless of whether they operate in a sector traditionally associated with national security. That said, the development of a national data policy provides an opportunity for the Australian government to provide clarity to investors on its concerns, and the conditions likely to be imposed, which will increase certainty for investors in these attractive sectors.

### More Information

For more information, please contact Natalie Bryce at [natalie.bryce@hsf.com](mailto:natalie.bryce@hsf.com)



# Foreign investment in the Australian financial sector: Drivers and regulation

Australia's financial services sector has seen significant M&A activity in the past few years, with financial institutions responding to uncertainties in the regulatory environment by focusing on their core businesses and divesting so-called 'non-core' businesses, such as life insurance and wealth management.

In this article, we explore the approval framework for foreign investors looking to acquire significant stakes in Australian financial services entities.



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## M&A activity and foreign interest expected to continue

M&A activity in the sector is expected to continue, particularly as greater clarity of the potential impacts of the Banking Royal Commission emerges.<sup>30</sup>

We also anticipate that foreign investors will continue to see Australia's financial sector assets as attractive offerings. As we have seen in the past few years, foreign bidders have been involved in all major deals in the sector, with AIA, Zurich, TAL Dai-ichi and Resolution Life each having agreed to acquire local life insurance businesses.

## What foreign investment approval is required?

Share acquisitions of prudentially regulated financial institutions, including by foreign investors, are regulated under the *Financial Sector (Shareholdings) Act 1998* (Cth) (**FSSA**).

Under the FSSA, approval from the Federal Treasurer is required before any person (both foreign and domestic) can acquire 15%<sup>31</sup> or more of a 'financial sector company'.<sup>32</sup>

Generally speaking, where a share acquisition is subject to the FSSA, it is exempt from the *Foreign Acquisitions and Takeovers Act 1975* (Cth) (**FATA**) which is the primary legislation regulating foreign investment into Australia. This exemption was introduced in 2015 as part of the re-write of Australia's foreign investment frameworks but does not extend to acquisitions by a foreign government investor. For foreign government investors, approval will be required under both the FATA and the FSSA.

## Is there any practical difference?

The decision maker under both the FSSA and the FATA is the Federal Treasurer, who has substantial decision making discretion under both Acts.

As a result, we expect there to be little or no practical difference between the approval criteria applied by the Federal Treasurer under either the FSSA or the FATA, particularly given that we would expect a high level of consultation between FIRB and APRA for approvals relating to financial sector companies.



30. The Royal Commission into the Misconduct in the Banking, Superannuation and Financial Services Industry.

31. Draft legislation was released in 1998 to increase the 15% ownership limit to 20% in line with the FATA.

32. A 'financial sector company' under the FSSA is an authorised deposit-taking institution, an authorised insurance company or a holding company of either.



Nevertheless, we have set out below the key differences between the FSSA and FATA.

	FSSA	FATA
Purpose of the legislation	<p>The FSSA was introduced in 1998 as the Government’s response to the 1997 Australian Financial Systems Inquiry.</p> <p>The focus of the FSSA is to create a diversity of ownership so that the financial health of a prudentially regulated financial institution is not dependent on the financial wellbeing of one person and/or their associates.<sup>33</sup></p>	<p>The FATA is the primary legislative framework for foreign investments into Australia.</p> <p>The focus of FATA is maintaining a welcoming environment for foreign investment that is not contrary to Australia’s national interest.<sup>34</sup></p>
National interest test	<p>This is a positive test requiring the Federal Treasurer to be satisfied that the acquisition is in the national interest.</p> <p>‘National interest’ is not defined in the Act, though it is relevant to refer to the stated objective of the FSSA, which is to minimise the risks associated with the concentration of ownership in Australian financial institutions.</p>	<p>This is a negative test where the Federal Treasurer may prohibit a transaction if it is found to be contrary to the national interest.</p> <p>Australia’s Foreign Investment Policy provides guidance on ‘national interest’ considerations which the Federal Treasurer will have regard to, being the impact of the investment on national security, competition, tax and other regulations, the Australian economy, the community and the character of the investor.</p>
Relevant advisory body	APRA	FIRB

**What it means for foreign investors**

We expect that the key drivers for M&A activity in the financial sector will continue to create investment opportunities for foreign investors.

The potential increase in regulation as a result of the Banking Royal Commission will no doubt play a role in driving some of this M&A activity, and it remains to be seen whether the Federal Treasurer will also impose further criteria for foreign investment in the sector. For example, greater focus may be placed on the character and reputation of the foreign investor and their ability to demonstrate proper governance and a culture of regulatory compliance.

**More information**

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33. See explanatory memorandum to the *Financial Sector (Shareholdings) Bill 1998* (Cth) at 1.

34. See explanatory memorandum to the *Foreign Acquisitions and Takeovers Legislation Amendment Bill 2015* (Cth) at 7.

# Foreign investment in 2019

Following a 7 year high in M&A activity in Australia, we consider recent changes to the FIRB legislation affecting foreign investors and look forward to the remainder of 2019 for trends and developments.

## Recent legal changes

Foreign persons with existing interests in Australian media, and any overseas entities looking to invest in Australian industries, should consider the following recent key changes to the FIRB legislation.

### Reporting requirements for foreign owners of media assets

Following the enactment of the *Broadcasting Legislation Amendment (Foreign Media Ownership, Community Radio and Other Measures) Act 2018* (Cth), there is now a requirement for foreign persons holding interests of at least 2.5% in Australian media companies to notify the Australian Communications and Media Authority (ACMA) of those interests.

This reporting requirement came into force on 1 September 2018, and if any foreign persons held a relevant interest in an Australian media company at that time, it was necessary for those persons to disclose their interests to ACMA by 28 February 2019. This amendment will also mean that incoming investors will need to disclose their interests in media companies within 30 days of any acquisition, while outgoing investors will need to advise ACMA of any interest disposal or change.

### Increase in screening threshold

As a result of the entry into the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), there are now increased screening thresholds for investors from CPTPP countries acquiring interests in mining and energy sectors (excluding uranium and plutonium extraction and nuclear facilities) and other non-sensitive businesses. Sensitive businesses include those in the military or telecommunications industries.

The thresholds for investments in these sectors have now increased from \$266 million to \$1,154 million. These changes will allow for easier investment in Australia for investors from any CPTPP participant nations. Since 30 December last year, the CPTPP has come into force for Canada, Japan, Mexico, New Zealand, Singapore and Vietnam. The heightened thresholds will also apply to Brunei Darussalam, Chile, Malaysia and Peru once these nations have each ratified the CPTPP.

## Looking forward to 2019

For the balance of 2019, we anticipate further foreign direct investment (FDI) in Australia by pension funds and sovereign wealth funds following the bumper year in M&A activity in Australia in 2018. The key sectors to watch are healthcare,<sup>35</sup> property, financial services and greenfield infrastructure. FIRB recently approved the takeover of Healthscope by way of scheme of arrangement by Brookfield, a Canadian investment group, showing positive signs for FIRB's approach to these kinds of transactions – which we only expect to become more common.

Moving forward, FIRB has called out several 'areas of focus' in its recent Regulator Performance Framework Report, including the improvement of 'customer service standards' and 'external client-facing systems and forms' and better turnaround times.<sup>36</sup> In any event, increased FDI and M&A activity in 2019, as one might expect, will necessitate greater oversight by FIRB. As evidenced by FIRB's rejection of the proposed takeover of APA Group by Hong Kong listed CK Infrastructure Group, we can expect continued regulatory scrutiny over acquisitions in major infrastructure this year.<sup>37</sup>



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As a federal election has now been called, FIRB has moved into caretaker mode which will delay FIRB applications during May and June 2019. We will also need to monitor any potential foreign investment policy changes in the event of a change in government. However, we do not anticipate any material policy changes in the short term, in the event of a change in government.

### More information

For more information, please contact Matthew FitzGerald at [matthew.fitzgerald@hsf.com](mailto:matthew.fitzgerald@hsf.com)

35. See N Bryce and C Walker "Foreign investment in data intensive sectors: FIRB's role in protecting Australia's data".

36. See 2017-18 Regulator Performance Framework Report at <http://firb.gov.au/about/publication/2017-18-regulator-performance-framework-report/> at 6 and 7.

37. See D Ryan and B Walker "Case study: FIRB's Rejection of Proposed Takeover of APA Group by CKI".





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