COMMENTS BY THE GOVERNMENT OF MEXICO TO THE AUSTRALIAN TREASURY

Foreign Investment Reform (Protecting Australia's National Security) Bill 2020

Submitted by:

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Foreign Investment Reform (Protecting Australia's National Security) Bill 2020
Agency: Australian Treasury

On behalf of the Government of Mexico, and regarding the exposure draft of the Foreign Investment Reform (Protecting Australia's National Security) Bill 2020 (the draft Bill), we submit the following comments.

The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) intends to "[e]stablish a predictable legal and commercial framework for trade and investment through mutually advantageous rules"[1].

To achieve this, all Parties to the CPTPP are bound to comply to the fullest with the provisions set out in Chapter 9, unless a Non-Conforming Measure in Annex I or Annex II allows otherwise. Notwithstanding, even in the case that a Non-Conforming Measure is inscribed in Annex I of the CPTPP, the Parties must observe the standstill and ratchet mechanisms and refrain from adopting new or more restrictive measures than those which were in place when the CPTPP entered into force[2].

In this regard, Australia's schedule of Non-Conforming Measures to Annex I includes the following entry[3] (Australia's NCM):

Sector:	*All*
Obligations Concerned:	*National Treatment (Article 9.4)*

[1] Preamble of the CPTPP.
[2] Annex II of the CPTPP lists specific sectors or activities where Government action is not constrained by the ratchet and standstill principles, thus allowing the parties to preserve flexibility in such sensitive sectors and activities.
[3] Annex I–Australia–3 through Annex I-Australia-6

	Senior Management and Board of Directors (Article 9.11)
Level of Government:	*Central*
Measures:	*Australia's Foreign Investment Policy, which consists of the Foreign Acquisitions and Takeovers Act 1975 (FATA) (Cth); Foreign Acquisitions and Takeovers Regulations 1989 (Cth); Financial Sector (Shareholdings) Act 1998 (Cth); and Ministerial Statements.*
Description:	*Investment* *1. The following investments[1] require notification and approval from the Australian Government:* *(a) proposed investments by foreign persons in existing[2] Australian businesses, or prescribed corporations,[3] the value of whose assets exceeds $A252 million* in the following sectors:* *(i) the telecommunications sector;* *(ii) the transport sector, including airports, port facilities, rail infrastructure, international and domestic aviation and shipping services provided either within, or to and from, Australia;* *(iii) the supply of training or human resources, or the*

manufacture or supply of military goods, equipment or technology, to the Australian or other defence forces;

(iv) *the manufacture or supply of goods, equipment or technologies able to be used for a military purpose;*

(v) *the development, manufacture or supply of, or provision of services relating to, encryption and security technologies and communication systems; and*

(vi) *the extraction of (or rights to extract) uranium or plutonium, or the operation of nuclear facilities;*

(b) *proposed investments by foreign persons in existing Australian businesses, or prescribed corporations, in all other sectors, excluding financial sector companies[4], the value of whose total assets exceeds $A1,094 million*;*

(c) *proposed direct investments by foreign government investors, irrespective of size;*

(d) *proposed investments by foreign persons[5] of five per cent or more in the media sector, regardless of the value of the investment;*

(e) *proposed acquisitions by foreign persons of developed non-residential commercial real estate where the property is valued at more than $A1,094 million*.*

Notified investments may be refused, subject to interim orders, and/or approved subject to compliance with certain conditions. Investments referred to above for which no notification is received may be subject to orders under Sections 18 through 21 and 21A of the FATA.

Separate or additional requirements may apply to measures subject to other Annex I reservations and to sectors, sub-sectors or activities subject to Annex II.

2. The acquisition of a stake in an existing financial sector company by a foreign investor, or entry into an arrangement by a foreign investor, that would lead to an unacceptable shareholding situation or to practical control[6] of an existing financial sector company, may be refused, or be subject to certain conditions.[7]

[Footnotes]

[1] Foreign Acquisitions and Takeovers Act 1975 (Cth) (FATA). "Investments" means activities covered by Part II of FATA or, where applicable, ministerial statements on foreign investment policy.

Funding arrangements that include debt instruments having quasi-equity characteristics will be treated as direct foreign investment.

[2] For the purposes of this entry, "existing" means in existence at the time the investment is proposed or made.

[3] For the purposes of this entry, "prescribed corporation" means:

(a) a trading corporation;

(b) a financial corporation;

(c) a corporation incorporated in a Territory under the law in force in that Territory relating to companies;

(d) a foreign corporation that, on its last accounting date, held assets the sum of the values of which exceeded $A252 million (for item (a) of the entry) or $A1,094 million (for item (b) of the entry), being assets consisting of all or any of the following:

(i) land situated in Australia (including legal and equitable interests in such land);

(ii) mineral rights;

(iii) shares in a corporation incorporated in Australia;

(e) a foreign corporation that was, on its last accounting date, a holding corporation of an Australian corporation or Australian corporations, where the sum of the values on that date of the assets of the Australian corporation or Australian corporations exceeded $A252 million (for item (a) of the entry) or $A1094 million (for item (b) of the entry);

(f) a corporation that was, on its last accounting date, a holding corporation of a foreign corporation referred to in paragraph (d) or (e) of this footnote;

(g) a foreign corporation that, on its last accounting date, held assets of a kind or kinds referred to in paragraph (d) of this footnote, where the sum of the values on that date of those assets was not less than one-half of the sum of the values on that date of the assets of the foreign corporation and of all the subsidiaries of that corporation; or

(h) a foreign corporation that was, on its last accounting date, a holding corporation of an Australian corporation or Australian corporations, where the sum of the values on that date of the assets of that Australian corporation or those Australian corporations was not less than one-half of the sum of the values on that date of the assets of the foreign corporation and of all the subsidiaries of that corporation.

[4] *A "financial sector company" means, as defined in section 3 of the Financial Sector (Shareholdings) Act 1998 (Cth):*

(a) an authorised deposit-taking institution;
(b) an authorised insurance company; or
(c) a holding company of a company covered by paragraph (a) or (b) of this footnote.

[5] *A "foreign person" means, as defined in section 5 of the FATA:*

(a) a natural person not ordinarily resident in Australia;
(b) a corporation in which a natural person not ordinarily resident in Australia or a foreign corporation holds a controlling interest;
(c) a corporation in which two or more persons, each of whom is either a natural person not ordinarily resident in Australia or a foreign corporation, hold an aggregate controlling interest;
(d) the trustee of a trust estate in which a natural person not ordinarily resident in Australia or a foreign corporation holds a substantial interest; or
(e) the trustee of a trust estate in which two or more persons, each of whom is either a natural person not ordinarily resident in Australia or a foreign corporation, hold an aggregate substantial interest.

[6] *"Unacceptable shareholding situation" and "practical control" as defined in the Financial Sector (Shareholdings) Act 1998 (Cth).*

[7] *Ministerial statements on foreign investment policy including the Treasurer's Press Release No. 28 of 9 April 1997.*

** This is the figure as at 1 January 2015. To be indexed on 1 January each year to the GDP implicit price deflator in the Australian National Accounts for the previous financial year.*

According to this, only the investments that surpasses the following monetary thresholds are subject to Australia's review process:

a) A $A252 million threshold for proposed investments by foreign persons in existing Australian business, or prescribed corporations in specific sectors and activities;
b) A $A1,094 million threshold for:

i. Proposed investments by foreign persons in existing Australian businesses, or prescribed corporations, in sectors, other than those mentioned in a) and financial sector companies;
ii. Proposed acquisitions by foreign persons of developed non-residential commercial real estate.

c) A zero-dollar threshold for:
i. Proposed direct investments by foreign government investors, irrespective of size;
ii. Proposed investments by foreign persons of 5% or more in the media sector[4].

Notwithstanding, several features of the draft Bill are inconsistent with Australia's obligations under the CPTPP. One of such features is the introduction of the concept of "*notifiable national security action*" to the Foreign Acquisitions and Takeovers Act 1975 (FATA).

The notion of "*notifiable national security action*" does not currently exist in the FATA, and will be created by the draft Bill with the intention to bind any foreign persons to notify the Treasurer of the acquisition of interest in a "*national security business*" or "*national security land*" [5], regardless of the value of the investment[6]. The lack of such

[4] These monetary thresholds are explicitly mentioned in the text of Australia's NCM. Their amounts may have increased, after Australia's commitment to index such amounts on 1 January each year to the GDP implicit price deflator in the Australian National Accounts for the previous financial year.

[5] The draft Bill does not include a specific definition of "national security business". It will be established by the regulations. The concept of "national security land" is included in paragraph (b) of the definition of "notifiable national security action". However, what constitutes an "Australian land" for the purposes of (b)(iii) will be left to a declaration by the Treasurer through legislative instruments.

[6] According to the Draft Bill, the term "**notifiable national security action** means any of the following actions taken, or proposed to be taken, by a foreign person:
(a) to acquire a direct interest in a national security business;
(b) to acquire an interest in Australian land:
(i) that, at the time of acquisition, is defence premises (within the meaning of section 71A of the Defence Act 1903, excluding subparagraph (a)(iii) of the definition of that expression); or
(ii) in which an agency in the national intelligence community has, or will have, an interest if, at the time of acquisition, the foreign person could reasonably be expected to be aware of the agency's interest or prospective interest; or
(iii) that, at the time of acquisition, is covered, in whole or in part, by an area of Australian land declared by the Treasurer by legislative instrument;
(c) to start a national security business."

notification or the realization of the action before receiving a no objection notification or an exemption certificate will be subject to criminal or civil penalties, or both.

This means that whenever a foreign person intends to perform an operation that involves an interest in the so-called "*national security business*" or "*national security land*", the screening thresholds of Australia's NCM will not apply. The Explanatory Memorandum to the draft Bill outlines such fact by stating "[a] *notifiable national security action is an action that is by its nature so likely to give rise to a national security concern that regardless of its size or value it requires review by the Treasurer*" (underline added).

Notwithstanding, the imposition of this new test would be inconsistent with the National Treatment provision of the CPTPP, and the aforementioned ratchet and standstill mechanisms.

Indeed, the National Treatment provision of the CPTPP prevents the Parties from discriminating between investors and investments of another Party and their own investors and investments, regarding their establishment, acquisition or expansion, among other activities[7]. However, the new national security test proposed by the Australian Government will unduly create such discrimination, for only "foreign persons" will be subject to the obligation to notify a "national security action"[8], thus imposing a new market access restriction and favoring Australian nationals.

Moreover, considering that the standstill and ratchet mechanisms allow the Parties of the CPTPP to liberalize their legal framework for foreign investment, but prevents them from imposing more restrictive measures, the cancellation of the $A252

[7] Article 9.4 of the CPTPP.

[8] On this, the Explanatory memorandum states: "National security businesses are endeavours that if disrupted or carried out in a particular way may create national security risks. This means that national security risks may arise if national security businesses are controlled or influenced by persons acting not in Australia's interests. For this reason it is important to enable the Treasurer to be able to review investments in such businesses by foreign investors" (underline added).

million and the $A1,094 million screening thresholds, when dealing with the so-called "*national security actions*", would constitute a transgression of such mechanisms.

A similar situation might occur through the "*reviewable national security actions*", which would allow the Treasurer to review a not significant action, notifiable action or notifiable security action, if the Treasurer considers that the action may pose a national security concern[9].

In this regard, the concept of "*reviewable national security action*" is also discriminatory, for it is only applicable to actions "*taken, or proposed to be taken, by a foreign person* [...]", according to the definition in Item 10, proposed Section 37B of the draft Bill. Hence, in the lack of evidence that Australian nationals would also be submitted to a similar test, the "*reviewable national security action*" would contradict the National Treatment provision of the CPTPP.

Also, as in the case of "*notifiable national security actions*", the "*reviewable national security action*" would apply to the establishment, acquisition or expansion of any investment, regardless of its size or value. In this case, it would suffice, that the Treasurer considers that the acquisition of a direct interest in an entity or an Australian business, or the acquisition of Australian land, among other activities, poses a national security concern, so that they are subject to this review, with the possibility that, in the end, the Treasurer prohibits the action. Thus, given that Australia did not included such review in its Schedules to Annex I or II of the CPTPP and, instead, it only locked-in the screening thresholds contained in Australia's NCM, such test would be contrary to the ratchet and standstill mechanisms, especially if they override Australia's NCM screening thresholds.

Additionally, it is important to notice that the "reviewable national security action" would not exclusively be a screening test. On the contrary, it would also apply to actions already taken in which case, "*the Treasurer may order that the action be undone*

[9] Draft Bill, items 7 and 10, 13, Sections 4, 37A, 37B and 37C of the FATA.

(for example, by requiring an acquisition to be disposed of)"[10]. In such situation, there would not only be a violation of the National Treatment provision and of the ratchet and standstill mechanisms, but there is also the risk that the exercise of such power by the Treasurer constitutes a violation of the fair and equitable standard of treatment and an indirect expropriation, for which compensation may be required.

Unfortunately, the transgression of Articles 9.6 (Minimum Standard of Treatment) and 9.8 (Expropriation and Compensation) of the CPTPP would not be limited to the exercise of the Treasurer powers linked to the "*reviewable national security actions*". Instead, it would also extend to the so-called "*last resort power*", whereby the Treasurer would have powers to impose conditions, vary existing conditions, or, finally, force the divestment of any realized investment where national security concerns are identified[11].

In this regard, as its name suggest, the "*last resort power*" takes place only when all other mechanisms have been satisfied and:

a) A person has been given a no objection notification in relation to the action;
b) A person has been given, or was taken to have been given, an exemption certificate in relation to the action;
c) An order or decision was not made in relation to the review of "reviewable national security actions", before the end of its decision period; or
d) A person was given a notice imposing conditions after the review of "*reviewable national security actions*".

Thus, when the "*last resort power*" takes place, the Treasurer's action might breach the legitimate expectations of investors, upon which they might have relied in deciding to make or maintain an investment, consequently opening up the possibility to give raise to a breach of the Minimum Standard of Treatment provision. Furthermore, if

[10] Draft Bill, item 13, Section 66 of the FATA.
[11] Draft Bill, items 13 and 39, Sections 66, 73A, 73B, 73D and 73F, among others.

the exercise of the "*last resort power*" results in the Treasurer ordering the termination of an existing agreement with an Australian business or the disposal of a direct interest in an entity, an Australian entity, an Australian Business, or in Australian land, it could constitute an indirect expropriation.

All of this, without even considering that empowering the Treasurer, in such broad terms, to direct a specified person "*to do a thing prescribed by regulations made for the purposes of this item*"[12] could lead to the transgression of other CPTPP provisions, such as Articles 9.10 (Performance Requirements) and 9.11 (Senior Management and Boards of Directors).

Mexico is aware that nowadays it is more necessary than ever to rethink national security protection schemes in light of the challenges that scientific and technical advances present and the changing international landscape.

However, both Australia and Mexico are linked by one of the most modern and ambitious treaties in the world, that has the objective of establishing a predictable legal and commercial framework for trade and investment through mutually advantageous rules, and that recognizes that the Parties should be able to adopt the measures that they consider necessary for the protection of their own security interests, as long as they do not derogate from the provisions of the Treaty itself[13].

In this regard, from our point of view, the introduction of the "*notifiable national security action*", the "*reviewable national security action*" and the "*last resort power*" to the FATA is inconsistent with Australia's obligations in the CPTPP and with the Parties' commitment to *"establish a comprehensive regional agreement that promotes economic integration to liberalise trade and investment [...]*".[14]

[12] Draft Bill, Item 13 and 39, Section 73F.
[13] Article 29.2 (Security Exceptions) of the CPTPP.
[14] CPTPP Preamble.

Therefore, we urge Australia to assess other options to achieve its legitimate objectives, which are consistent with the principles and provisions agreed upon by the Parties to the CPTPP and, accordingly, that do not impair the protections and liberalization measures afforded by such treaty.

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