Piper Alderman

Reforms Proposed in Foreign Investments

On 4 August 2009 the Treasurer, Wayne Swan, announced reforms to Australia's foreign investment screening framework by way of proposed amendments to the Foreign Acquisitions and Takeovers Regulations 1989. Corporate Lawyer, Bianca Battistella, reviews the proposals.

In an attempt "to attract a greater slice of international capital to Australia" and to "position Australia for a more competitive recovery beyond the global recession", the reforms will increase the monetary thresholds that trigger the requirement for the Foreign Investment Review Board (FIRB) to review certain investments in Australia by overseas investors.

The effects of the changes are as follows:

- the four lowest thresholds for private foreign investment in Australian business will be replaced with a single threshold of 15% in a business valued at $219 million (from as little as $100 million under current regulations), meaning that investment in businesses valued below $219 million can proceed without review
- the new threshold will be indexed on 1 January each year to prevent foreign investment screening from becoming increasingly restrictive over time
- the requirement that private non-United States investors notify the Government when establishing a new business in Australia valued above $10 million will be abolished.

An exception to this new threshold is that investment in non-sensitive sectors by United States investors will continue to be exempt from review if the business is valued at less than $953 million.

The FIRB regime in relation to investment by foreign governments or state-owned or controlled enterprises will also remain unchanged, requiring prior FIRB approval in all cases, irrespective of the value of the investment.

Moreover, there is no change proposed to the Australian urban land provisions or the media sector rules. It is important to remember that all acquisitions of Australian urban land will continue to be subject to FIRB review.

Given the benefits generated by foreign investment in Australia, such as the creation of greater activity in the Australian economy and employment opportunities, the proposed reforms are aimed at improving Australia's competitiveness as a place to invest and reducing the associated disincentives, most notably being unnecessary compliance costs and delays.

The Federal Government had received many applications for the establishment of businesses worth more than $10 million but not a single new business proposal has been rejected for more than a decade. The proposed measures are considered by the Treasurer to be important in ensuring that the Government does not become unnecessarily involved in uncontroversial business transactions.

The Government believes that, as a consequence of these changes, approximately 20 per cent of all business applications will no longer be subject to screening by the FIRB.

Despite the proposed changes being described by trade experts as "the most significant liberalisation of our foreign investment policy since the United States-Australia free-trade agreement" in 2005, some commentators have openly criticised the maintenance of the Treasurer's discretionary power to block foreign takeovers "in the national interest" and the secrecy of FIRB's investment deliberations.

Further, the Treasurer has denied that the amendments could discriminate against Chinese investment in Australia, given China's focus on investment by state-owned enterprises, claiming that we "welcome Chinese investment" in Australia.

Directors and their Adviser found Liable in Relation to Phoenix Activity

Corporate Law Graduate, Paul Henry, discusses the recent decision of the Supreme Court of New South Wales in ASIC v Somerville in which the Court considered the potential liability of professional advisers in the context of artificial arrangements concerning corporate reorganisations.

On 8 September 2009, in an action brought by the Australian Securities and Investments Commission (ASIC), Acting Justice Windeyer of the Supreme Court of New South Wales found that Mr Timothy Donald Somerville, a solicitor, contravened the *Corporations Act 2001* (Cth) (Act) by assisting eight directors of unrelated companies to breach the Act by engaging in what ASIC regards as illegal "phoenix activity".

Phoenix activity involves a director transferring the assets of an indebted company to a new company of which he or she is also a director. The new company continues to operate while the director places the indebted company into administration or liquidation with no assets to pay creditors. Simply put, it is an attempt to transfer the assets of an indebted company away from the reach of creditors.

In this case, each director had sought the advice of Mr Somerville as to the company's position and the available courses of action in circumstances where the original company was suffering or was about to suffer financial problems. While each company may not have necessarily been insolvent at the time, it was under the threat of insolvency or at least likely to become insolvent.

The same pattern emerged in each of the transactions concerning the different companies:

- the old company ceased to trade
- a new company was formed, usually with a similar name
- an agreement was entered into between the new company and the old company whereby the old company transferred all of its assets to the new company as consideration for shares issued by the new company.

The consideration offered for the transfer of the assets was in every case the issue of 100 "V" class shares in the purchaser company. The "V" class shares were non-voting shares that carried the right to receive all dividends declared by the company until a total amount (supposedly the value of the transferred assets) was paid.

In no case was a dividend paid on the "V" class shares.

Acting Justice Windeyer confirmed the well established principle that where a company is insolvent, or might be insolvent, or is nearing insolvency, the directors owe a duty of care to the creditors of the company which cannot be overridden by shareholders and which needs to be taken into account by the directors in dealing with the assets of the company in question.

His Honour found that "What has really happened here is that a scheme has been devised to bring about asset stripping but to attempt to make this seem legitimate by providing for "V" class shares". His Honour accordingly found that each of the eight directors had contravened:

- section 181(1) of the Act (the duty to act in good faith and for a proper purpose) – there was no proper basis for the transactions other than to keep the benefit of the assets in another company without the burden of liabilities
- section 182(1) of the Act (the duty to not use their position improperly) – the directors gained an advantage for themselves as they continued to direct companies which had the use of the transferred assets and they benefited the new company
- section 183(1) of the Act (the duty not to use information improperly) – the transfers took place, using the knowledge that the vendor company was insolvent or nearing insolvency, to give an advantage to the directors which caused detriment to the vendor company in circumstances where the interests of creditors needed to be considered.

Further, and significantly, his Honour found that Mr Somerville had contravened section 79 of the Act. Section 79 provides that a person may be liable for involvement in a contravention of the Act where the person has aided, abetted, counselled or procured the contravention, has induced the contravention, has in any way, by act or omission, directly or indirectly, been knowingly concerned in or a party to the contravention, or has conspired with others to effect the contravention.

In this case, Mr Somerville advised and recommended the transactions which resulted in the breaches, prepared all the documents necessary to carry out the transactions, and arranged the execution of the documents with knowledge of the relevant facts. His Honour found that in doing so it was clear that Mr Somerville aided, abetted, counselled and procured the carrying out of the transactions.

It was accepted that not all advice will result in liability under section 79 of the Act. However, his Honour stated that in this case "There was a direct causal connection between his involvement and the breach. I find the transactions would not have taken place but for his involvement". Accordingly, Mr Somerville was liable under section 79.

This is the first time ASIC has been successful in taking action against an adviser under section 79 for their role in facilitating phoenix activity. While the case concerned a solicitor, there is nothing in the judgment, or the statutory provisions, that prevents a similar finding being made against other advisers. Whether an adviser will be held liable will depend upon the nature and extent of that adviser's involvement in a proposed transaction, and the nature and terms of that transaction.

This case is a reminder to directors and their advisers of their responsibilities in an insolvency, or near insolvency context to carefully consider whether they are complying with statutory and other duties imposed on them.

Great Barrier Reef Protection to be the Subject of New Laws

The Great Barrier Reef Protection Amendment Bill 2009 (Qld) was introduced to Queensland Parliament on 4 June 2009 with the majority of its provisions proposed to commence on 1 January 2010. Property & Projects Senior Associate, Nick Prove, and Law Clerk, Alisha Deveson, review the Bill.

The principal objective of the Bill is to introduce a regulatory structure to reduce the impact of agricultural activities on the water entering the Great Barrier Reef.

The Bill will affect around 4,500 property owners in the Mackay-Whitsunday region, and the Burdekin Dry Tropics and the Wet Tropics, as the highest levels of water pollution have been found closest to these catchment regions. The principal aim is to regulate the amount of fertilisers and pesticides used, particularly by sugar cane farmers and graziers.

Summary of major changes -

1. Limiting the regulatory net to the three specific high priority catchments
2. Regulating the two agricultural sectors (cattle and cane) that contribute the highest levels of chemicals and sediment found in Reef waters
3. Adopting standard minimum requirements for all properties where possible
4. Containing the environmental risk management plan (ERMP) requirements, initially to the highest priority activities with thresholds based on property size, with a further mechanism to enable ERMPs to be required in other identified hot spots.

The Bill introduces the concept of an “agricultural environmentally relevant activity” (ERA) and will require “high risk” farms to keep ERMPs.

It is estimated that 1,000 farms in the Wet Tropics and Burdekin Dry Tropics which are considered high risk to the Reef will be required to prepare an ERMP to entrench the adoption of best practices and continuous improvement, leading to better Reef health. The ERMPs are to show that the farms are improving their practices, specify the size of the landholding, state the type and quantity of pesticides and fertilisers used, the soil testing being undertaken, and stocking rates.

The legal regime is a mix of strict controls that will improve farming practices at the least cost to taxpayers. The Premier of Queensland has set a target of reducing the levels of dangerous pesticides and fertilisers found in Reef waters by 50 per cent over the next four years, which the Bill is designed to achieve.

Significantly the Bill does not classify an “agricultural ERA” as a “Material Change of Use” under the *Integrated Planning Act 1997* (Qld) and therefore does not trigger the requirement for a development approval for these activities.

The cost and benefits will vary from farmer to farmer. Those farmers who already keep a management plan through applying correct levels of fertiliser, using pesticides responsibly and taking measures to minimise Reef run-off will not be greatly affected. However, those farmers who currently have no management plan will need to change how they operate in order to comply with the new laws and regulations.

Food and Juice Labelling Laws get the Squeeze

A Private Members Bill, introduced by Nick Xenophon on 20 August 2009, seeks to tighten up laws relating to the circumstances when food and juice products can claim to be "Australian Made". Corporate Partner and Head of the firm's Agribusiness Practice Group, Simon Venus, and Associate, Will Fennell, take a preview of the Bill and the proposed new regime.

Post farm gate value adders in the food and beverage sectors should be aware of the proposed new legislation which will impact on food labelling. While not necessarily supported by the sector, the proposed legislation is indicative of a populist move to amend food and beverage labelling in Australia.

Independent Senator Nick Xenophon's private bill, the Food Standards Amendment (Truth in Labelling Laws) Bill 2009, seeks to insert a new section 16A into the Food Standards Australia New Zealand Act 1991. The Bill will require the regulatory authority known as "Food Standards Australia New Zealand" to develop labelling standards to limit the use of the word "Australian" to food 100% produced in Australia.

The labels on food containing imported ingredients will be required to declare the inclusion of imported ingredients, in text no less than 15mm on the front label of the relevant food. In the case of juices, products containing imported ingredients will be required to display the percentage amount of imported ingredients in letters not less than 25mm on the product container's front label. The product container and product label are not to be taken into account in determining the percentage of Australian content. Further, juices containing concentrate must disclose this fact to consumers in similar labelling.

The Bill also prevents drinks partly or wholly produced from orange skins being described as "orange juice".

According to Senator Xenophon, *"Right now, you can label a fruit juice as 'Made in Australia' even if half the juice comes from overseas – as long as the box and label are locally made"*. Notwithstanding, the Bill does not include the product container or product label in any calculation of percentage of Australian content in a product. Accordingly, under the proposed regime a product could be wholly Australian sourced yet use packaging derived from overseas, and still be labelled "Australian Made".

The current labelling regime is governed by sections 65AA to 65AN of the Trade Practices Act 1974. These provisions require that products represented to be "Made in Australia" must be substantially transformed in Australia with at least 50% of the cost of production incurred here. Products may use the term "Product of Australia" if they are 100% made in Australia from all or nearly all Australian ingredients. The Australia New Zealand Food Standards Code also applies, however, the provisions of this code largely mirror the Trade Practices Act provisions.

Whilst the distinction made in the Trade Practices Act introduced by the Liberal Government in 1998 may appear straightforward enough, according to Greens leader Bob Brown, the advertising campaign undertaken to educate consumers as to the difference between "Product of Australia" and "Made in Australia" "has failed and consumers continue to be confused and misled by labels".

According to Senator Brown, research undertaken by Roy Morgan in late 2006 found that Australian consumers want to buy Australian and that more than two thirds consciously do "whenever possible" or "often". Senator Brown said that buying Australian was both good for the economy and the environment. "Buying locally grown and produced food means profits and jobs stay in Australia. An increasing reliance on the long distance transport and refrigeration of foods that are grown thousands of kilometres away impacts heavily on our carbon footprint. Buying local, Australian products is often more convenient and the food is fresher and better tasting".

Senator Brown previously attempted to move a similar Bill through the Senate in 2003 and again in 2005, however such moves failed. Accordingly, Senator Brown and the Australian Greens are co-sponsoring the bill together with Senator Xenophon.

According to Senator Xenophon, the confusion surrounding fruit juice labelling at the present time allows large foreign owned juice companies to pass off significantly foreign juices as “Made in Australia” and then pocket the difference.

In his Second Reading speech to Parliament, Senator Xenophon claimed to have received many submissions from Riverland fruit growers to the effect that the current labelling regime significantly contributes to the serious challenges those farmers face. Senator Xenophon stated that Riverland growers and primary producers want a system whereby “Made in Australia” means precisely that, produce totally made in Australia from Australian produce. According to Senator Xenophon “allowing foreign fruit to be effectively hidden in juices that call themselves ‘Australian made’ for example, hurts demand for their produce and is contributing to unsustainable prices”.

However, there are a number of opponents to the Bill. Australian Food and Grocery Council Chief Executive Kate Carnell says “Extending this requirement to 100 per cent of products makes no sense and will mean that virtually no food manufactured in Australia will be able to use the term “Australian Made” due to the use of small amounts of imported additives, flavours or colours”. Ms Carnell noted that certain raw materials and additives are only available from overseas sources, citing the example of cocoa used to make well known Australian chocolate products. Ms Carnell also said that Senator Xenophon’s “proposed Bill demonstrates a populist and short-sighted approach to food labelling” and that the Bill is at odds with existing food standards.

The Selection of Bills Committee has recommended the Bill be referred to the Economics Legislation Committee. It is expected the Economics Legislation Committee will produce a report mid-November 2009. Piper Alderman will update e-bulletin readers with the outcome of the Committee report and the progress of the Bill.

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