

Governmental Approval Process of Chinese Investment into  
Australian Energy and Resources

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1. Introduction

The past years has seen a substantial increase in number of transactions in which Chinese entities, especially State Owned Enterprises (SOE or SOEs), are actively investing in Australia energy and resources assets. Huge transactions, like the 19.5 billion USD deal between Chinaclo and Rio Tinto which is still pending at FIRB, have received attention and concerns from all walks of life in Australia as well as in China.

Aimed at securing the increasing demand of energy and resources consumption of its growing economy, China's central government has become more and more actively in

implementing the "Go-abroad" Strategy ("Zouchuqu Zhanlve"). To ensure that PRC companies 'actively and safely' carry out outbound investment, one of the Chinese outbound investment regulators, MOFCOM, has released the Administration Measures on Outbound Investment (New Measures), which came into effect on 1 May 2009. From the perspective of China, outbound investment in energy and resources area will benefit the sustainable development of China's economic growth and ultimately, promote the global peace, prosperity and public welfare.

Meanwhile, foreign direct investment is an important tool for building wealth and economic prosperity in Australia. It helps create jobs in the host country, facilitates economic expansion and contributes to productivity-enhancing investment in machinery, equipment and infrastructure such as road, rail and ports. For these and other reasons, most countries, including Australia and China, are eager to attract inbound investment from overseas.

At the same time, however, many feel uncomfortable with the idea of foreign ownership of a significant share of domestic business. As we have seen, the press, the people and the government of the host state have been increasingly careful and cautious in dealing with cases where the foreign investor is controlled by a foreign government and the business to be sold is of strategic importance. It is argued that foreign government controlled enterprises may not always act in the national, or local, interest; that one government shall not sell its own strategic assets to another sovereignty; and that foreign governmental ownership could have more national security implications in cases where products or industries are of strategic importance. These concerns tend to be most pronounced in the energy and natural resource sectors.

For these reasons, countries tend to make stricter and closer scrutiny on foreign governmental investors before granting access to domestic energy and resources sector. In addition, numerous countries have in place a screening process that reviews all major proposed foreign direct investments in order to determine whether they serve the national interest.

Part 2 of this report provides a detailed description of the review process as well as an analysis of possible impact on Chinese investment into Australia energy and resources

sector. The review process has been updated by MOFCOM, the PRC regulator on outbound investment of Chinese entities, since the new Measures came into force on 1 May 2009.

Part 3 describes the general foreign investment screening process in Australia, with an emphasis on the Six Principles taken by the FIRB and the Treasurer in considering proposals from foreign governmental investors.

Finally, the conclusion then summarise the above comparative analysis and sequentially, some proposed solutions are set out hereto.

## 2. Chinese Side: New Outbound Investment Approval Process of MOFCOM

### 2.1 Major Actors of China in Outbound Investment Law and Policy Making

Various ministries and commissions under the State Council, the powerful PRC central government, are involved in regulating and promoting the increasingly active outbound investment. Namely, the National Development and Reform Commission is in charge of making industrial directory for investing abroad, the Ministry of Finance for the tax favoured policy supporting overseas investment and the Ministry of Commerce for the approval of individual outbound investment projects. Among them, (MOFCOM), is currently deemed as the most influential one. Subparagraph 2.2 draws out a big picture of how the MOFCOM approval process should be under the Administration Measures on Outbound Investment (New Measures).

### 2.2 MOFCOM and the Administration Measures on Outbound Investment

As mentioned above, it is generally believed that MOFCOM's leading role has been significantly highlighted when the New Measures came into effect on 1 May 2009 and the previous MOFCOM regulations on PRC outbound investment, The Provisions on the Review and Approval of Outbound Investment to Establish Enterprises, released 1 October 2004 (2004 Regulations), were repealed from the same date.

The New Measures, by introducing the approval, reviewing and granting and expiry system the Overseas Investment Certificate (Certificate), has strengthen the role of MOFCOM in regulating outbound investment. A Certificate will be granted to the

PRC company once MOFCOM has approved an outbound investment application. The PRC company must provide that Certificate for foreign currency, banking and customs procedures, and may be entitled to supporting policies of the PRC, such as preferential loans or access to markets. Unlike the 2004 Regulations, under the New Measures the Certificate expires automatically in two years following the date on which the Certificate is granted. This is unless the PRC investor has completed the relevant domestic or overseas legal procedures for the outbound investment within that two year period.

Interestingly, the New Measures set out clearly that where an application for outbound investment is rejected by MOFCOM, MOFCOM must notify the applicant in writing explaining the reasons for the rejection. Additionally, the applicant is entitled to apply for reconsideration of the application or may bring an action in court to challenge MOFCOM's decision. All these will make a rejection decision more difficult than an approval one, underlying the legislators' aim at promoting outbound investment by PRC companies.

### 2.3 Conclusion: Approval process simplified and more certainty achieved

PRC outbound investors have been concerned about the red tape procedure they have to go through before ultimately obtaining the approval and the uncertainty of the timeline of the process. Also, the above-mentioned concerns mean substantially for Australian mining companies who have urgent need for inbound investment from China, especially when facing such an unprecedented financial crisis. Therefore, more meaningfully for both PRC outbound investors and Australia companies who are interested in seeking PRC investment, the New Measure has simplified the approval process and improved the certainty in timeline of process. Firstly, to facilitate PRC companies, especially those from non Beijing-based private sectors, undertaking outbound investment, particularly in the mining and resources area, MOFCOM has delegated a large portion of its review and approval powers to its provincial branches. Consequently the national MOFCOM will only review large or politically sensitive investment projects. Secondly, there is now, in the New Measures, a more definite time frame in which MOFCOM is required to finalise its decision. That is, MOFCOM

itself shall complete the review process in 30 business days and the provincial MOFCOM shall reach the final decision in 20 business days.

### 3. Review of the Foreign Governmental Investment into Energy and Resources in Australia

#### 3.1 Regulator

Under Foreign Acquisition and Takeover Act 1975(FATA) and the regulation of FATA, the Treasurer is responsible for foreign investment policy and for making decisions on individual investment proposals. The FIRB is a non-statutory body that advises the Australia Government on foreign investment issues and administrators the legislation that regulates foreign investment. Therefore, FIRB's role is advisory only.

#### 3.2 Foreign Investment Policy and Legislation

Foreign investment in Australia is governed by policy and legislation. Foreign investment policy is reinforced, but not completely covered by: (1) Foreign Acquisitions and Takeovers Act 1975 (Cth);(2) Foreign Acquisitions and Takeovers Act 1989 (Cth) and (3) Foreign Takeovers (Notices) Regulations (Cth).

Generally, compulsory FIRB approval is required for all investments made by foreign entities seeking to acquire Australian assets where the target Australian company or assets are valued at AUD 100 million or more and the foreign entity is acquiring 15% or more of the Australian company or assets. Compulsory FIRB approvals in these circumstances are a legal requirement.

However, as a result of the new guidelines announced on 17 February 2008, ALL proposed investments by foreign government and their agencies must receive FIRB approval. An important exception to requiring FIRB approval for a foreign investment is if the interest is acquired directly from the Australian Government.

#### 3.3 Specific rules for Foreign Governmental Investors

Reflecting Australia's escalating concerns about the national interest involved in investments by foreign governments and their entities, the Department of Treasury

has released a six-principle policy applied by the Foreign Investment Review Board (FIRB) when considering a proposal from a foreign governmental investors which include state-owned enterprises (SOE) and sovereign wealth funds (SWF):

- (1) Whether the Acquirer's operations are independent from the foreign government?
- (2) Is the Acquirer subject to and does it adhere to the law and observe common standards of business behaviour.
- (3) Will the investment hinder competition or lead to undue control in the sector concerned (diversity of ownership and markets)
- (4) Will the investment impact on Australian Government revenue or policies?
- (5) Will the investment impact on Australia's national security?
- (6) Will the investment impact on the operations of an Australian business and will it contribute to the Australian economy and community.

It is notable that the legal nature of the above-listed Six Principles shall be policy other than legislation. Since the policy has not been incorporated into Australia's law, they may not be strictly enforceable. Instead, the policy introduces 'rules', requiring the merits of each case to be considered. It also provides that the Treasurer (and FIRB) with a greater discretion, since he is both the policy creator and the decision maker. This may make the process more subjective than if it were a law and possibly less open to appeal, especially as policy is free from judicial review unless it is inconsistent with the law.

#### 3.4 Recent development: use of undertakings for conditioned approval

Since 17 February 2008 when the revised FIRB notes for SOE's were announced, no resource investment applied for by Chinese companies has been rejected. On the contrary, some significant transactions have been approved recently.

- (1) On 8 May 2009, Mr Swan approved the application by Anshan Iron and Steel Group Corporation (Ansteel) to acquire an additional shareholding in Gindalbie Metals Ltd, up to a maximum of 36.28 per cent, conditional upon legally enforceable undertakings by Ansteel.

(2) On 23 April 2009, the Treasurer approved Minmetals' assets acquisition proposal, conditional on Minmetals providing legally enforceable undertakings.

(3) Weeks earlier, on 31 March 2009, the deal between Hunan Valin and Fortescue got approved. Hunan Valin Iron and Steel Group for up to a 17.55 per cent shareholding in Fortescue Metals Group, subject to the formal and strict undertakings that the Treasurer has sought from Hunan Valin.

The above three approvals were granted on a conditional basis. The state owned entities were required to provide undertakings directed at, in the case of Minmetals and OZ Minerals, ensuring the Australian businesses acquired are operated in accordance with commercial objectives and that pricing of output is on arm's length terms and, in the case of Fortescue, managing conflicts arising from appointments to the Fortescue board.

### 3.5 Conclusion

- (a) The FATA is not fatal. Statistics shows that only a rather limited number of applications have been rejected.
- (b) There are no special rules for China. The Six Principle is not aimed at Chinese SOEs only. It is applied to any SOE or SWF from any country.
- (c) The increasing use of undertakings for conditioned approval demonstrate FIRB's willingness to use undertakings to manage any specific national interest concerns arising from a proposal, while ensuring Australia continues to benefit from foreign investment.

## 4. Conclusion

To circumvent the red tape FIRB approval, it is advisable to learn from Japan's experience, which did work in 1970's when Japanese companies were doing in similar manners as PRC companies are doing now. That is, PRC government shall encourage other than discourage Chinese private investors to do substantial overseas investment in Australia.

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