

# Taste of Australia

July 2024





Hamilton Locke's Taste of Australia provides foreign investors and their advisers with a snapshot of the issues that have been front of mind for deal makers in Australia during the last quarter. The information is deliberately introductory – no more than a taste. However, our experts would be delighted to expand on any aspect that may be of interest to you or to any of your clients.

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## Opposition goes nuclear

The battle lines are beginning to be drawn in the run up to Australia's next federal election.

The leader of the Liberal/National opposition surprised the market in June by announcing that their policy in government would be to meet Australia's 2050 net zero emissions commitment by building seven nuclear reactors on the sites of existing coal fired plants. He also expressed the view that Australia's 2030 emissions reduction targets could not be met by the incumbent Labor Government's plan to replace coal generated power with renewables alone.

The announcement sets up the next election as a referendum on energy. It is a striking development in a country that has no utility scale nuclear energy industry and has historically carried an anti-nuclear sentiment.

For their part, the Government remains strongly committed to renewables as the pathway to reaching Australia's net zero commitment. Only this week, the Government introduced into Parliament its omnibus 'Future Made in Australia' legislation to accelerate the penetration of renewable energy and decarbonisation technologies. We discuss those initiatives in our article below.

The leader of the opposition will be keen to frame the energy debate as a cost-of-living issue. He has admitted however that costings for a nuclear pivot could only be developed in government. It is therefore unlikely that the electorate will be considering a fully formed nuclear proposal before the next federal election (which must be held before September 2025). Instead, the debate will be won or lost through fundamental politics, namely on which party can best convince the electorate of its ability to tackle the household cost-of-living crisis. It is shaping to be a close race.

Some business commentators have expressed concern that the opposition's policy announcement could disrupt the flow of foreign investment into Australian renewables projects. However, the sheer scale of the energy transition challenge is likely to ensure that demand for renewables projects continues unabated. Research released recently by BloombergNEF suggests that even if 7 GW of nuclear energy (which is the number suggested by the opposition policy) comes online by 2050, an additional 170GW of utility scale solar and wind energy will still be required to reach net zero.<sup>1</sup> If those numbers are to be believed, renewables must remain a key plank in Australia's energy transition, irrespective of which political party is in power.

<sup>1</sup><https://www.afri.com/companies/energy/nuclear-power-would-do-little-to-reduce-need-for-renewables-report-20240627-p5jpd4>

## M&A and Capital Markets update

Activity in the mid-market remains strong as we continue to see investors look for cash generating investments with low capital requirements. We are finding investors remain particularly interested in professional services, software as a service and cloud or cyber security businesses. We are also seeing continued interest in the renewables, and agribusiness sectors.

The timeframes for initiating and finalising transactions remain extended as a result of the tight market conditions. Sellers are investing more time in getting their business 'sale ready' before inviting buyers into a process, as buyers and their funders are insisting on an increasingly thorough due diligence process. ESG (Environmental, Social, Governance) and cyber security remain prominent topics in due diligence processes.

There has been a slight uptick in public M&A transactions, with 22 transactions announced in the first quarter of 2024. Consistent with international trends, we are continuing to see a significant volume of take private transactions, driven by the availability of private capital and a growing sense that public markets are not providing full value for listed assets.

That being said, hopes for the IPO market were buoyed by the recent ASX listing of Mexican restaurant chain Guzman y Gomez which listed at a \$2.2 billion valuation and rose to over \$3 billion in early trading. Other market aspirants will be keeping a close eye on subsequent trading.



## Foreign investment update – you have been heard!

On 1 May 2024, the Australian Treasurer announced reforms designed to 'strengthen' and 'streamline' Australia's foreign investment framework. These were in response to feedback that aspects of the FIRB approval process had become irritants to foreign investment in Australia.

At the centre of the new reforms is a renewed risk-based approach to screening foreign investment proposals. Specifically, Treasury will endeavour to deliver faster approvals for 'low-risk' proposals including:

- proposals by investors who are well known to Treasury and who have a strong track record of compliance with Australia's foreign investment regime; and
- investments in non-sensitive sectors such as manufacturing, commercial real estate and professional services.

As a result, Treasury has committed to processing 50% of applications within the initial statutory timeframe of 30 days, from 1 January 2025. While that is a modest commitment, it would represent a marked improvement from current processing times.

In contrast, the following sectors have been flagged as being particularly sensitive and will be subject to greater scrutiny going forward:

- critical infrastructure;
- critical minerals;
- investments in proximity to sensitive Australian Government facilities and defence sites; and
- investments which involve holding or having access to sensitive data sets.

Treasury also announced an intention to bolster its compliance and enforcement function, to allow for increased enforcement of approval conditions. Treasury intends to increase its capacity to undertake site visits for this purpose and also flagged there will be an increased use of the Treasurer's call-in power.

Other notable reforms include a commitment to refund filing fees for applications submitted by unsuccessful bidders in competitive processes and lifting the prohibition on foreign investors acquiring established 'build to rent' properties.



## Compulsory merger notification regime announced

A long-running campaign by the Australian Competition and Consumer Commission (ACCC) has led to the introduction of a mandatory merger notification regime from 1 January 2026.

Under the new regime, a party seeking to acquire control of a business will be required to notify the ACCC if the transaction exceeds specified thresholds. While the detail of those thresholds has not yet been announced, they will be a combination of deal value, merger party turnover and/or market share measures. The ACCC has previously suggested surprisingly low thresholds of only A\$35 million in global deal value or acquirer/target turnover of only A\$400 million. If implemented, thresholds at those levels would capture dramatically more transactions than are currently notified to the ACCC voluntarily. It remains unclear precisely how acquisitions of minority interests will be handled under the applicable control test.

Importantly, all transactions of the buyer and seller within the previous three years will be aggregated for the purposes of determining whether a transaction meets the mandatory notification thresholds. Under this mechanism, creeping/serial acquisition and roll-up strategies may routinely trigger a notification requirement.

ACCC assessments will be conducted in two phases. The Government has indicated that the first phase is likely to be a 30 working day review, with the option of a “fast-track” clearance for uncontentious deals after at least 15 days. The clock will start only once the ACCC has accepted a complete notification, putting the onus on the parties to provide all the required information upfront. A second phase review, involving in-depth legal and economic analysis, will occur if the ACCC has a “reasonable basis to consider that the merger raises competition concerns” and will require another 90 working days.

All mergers reviewed by the ACCC will be listed on a public register, and while a potential buyer will be able to engage in confidential pre-notification discussions with the ACCC, it is unlikely that the current practice of seeking and obtaining ACCC clearance for uncontentious deals on a wholly confidential basis will continue. In practice that means filings will need to be made after announcement of the deal, pushing out transaction timetables accordingly.

It is proposed that the reformed system will impose fees of up A\$100,000, with a fee exemption for small businesses (currently undefined).

The ACCC will be required to clear a merger unless it “reasonably believes that the merger would have the effect, or likely effect, of substantially lessening competition in a market”. Again, transactions in the past three years will be aggregated for the purposes of applying this test. The existing “merger factors” in the legislation will be replaced with “principles” that focus on market structure, the conditions for competition, the market position(s) of the merger parties, and any entrenchment of market power. The expectation is that this will lower the bar for identifying substantive competition concerns, especially for small or serial acquisitions by larger players.

The Government will consult on exposure draft legislation to implement the reforms – including on the notification thresholds, timelines, fees and penalties – in the coming months.





## Real Property update

The Australian real estate sector continues to exhibit diverse trends across the various asset classes.

### *Residential*

The 2024 Federal Budget (**Budget**), which was announced on 14 May 2024, introduced several initiatives to address the ongoing residential housing crisis. An additional \$1 billion in funding has been allocated to the Housing Support Program to boost the delivery of new housing developments. Universities are now required to increase student accommodation to alleviate pressure on the rental market, as international student enrolments return to pre-pandemic levels.

As noted in our foreign investment update above, Treasury has lifted the prohibition on foreign investors acquiring established build-to-rent developments. It is hoped that this change in policy, coupled with a reduction in FIRB application fees for such investments, will encourage foreign capital to flow to that part of the market.

Residential rental growth remains robust, with annual rent growth at 8.5%. House prices are still surging, which has been driven by limited housing supply at a time of high demand, particularly in peripheral areas around the major CBDs. This has in turn led to low vacancy rates and increasing rents.

### *Retail*

In 2023, the retail property sector outperformed both the office and industrial sectors in transaction volumes. Despite the slower start in 2024, the retail sector is expected to continue to outperform, supported in part by income tax cuts that became effective from 1 July 2024.

Interestingly, regional shopping centres have shown the most resilience and are among the top performing retail assets across Australia, with a 5.8% increase in total sales compared to 2023.

### *Office*

Whilst five out of six Australian CBD markets recorded positive absorption in early 2024, the national CBD vacancy rate remains relatively flat. Submarkets on the fringe of the CBDs are benefitting from the flight to quality and demand for premium A-grade assets, which is keeping vacancy levels lower than the suburban locations.

This ongoing “flight to quality” trend has sustained demand for premium office space and CBD buildings, particularly in those areas with strong amenities and transport infrastructure.

Generally, there are limited new office developments with overall supply projected to be 50% below the 2023 levels due to the high construction costs and low pre-commitment activity.

### *Industrial*

The industrial and logistics sector has experienced a slowdown due to the high interest rates and lack of supply of warehouse space across Australia. Despite this, new supply reached 579,000m<sup>2</sup> in the first quarter of 2024, with Sydney and Melbourne accounting for the majority. Transaction volumes also increased for the fourth consecutive quarter, reflecting the steady demand for industrial and logistics assets despite the broader economic challenges.

### *Hotel*

The Australian hotel market is expected to maintain strong transaction volumes in 2024. The sector performed well in the first quarter of 2024, which was attributable to high-profile concerts and major sporting events in Sydney and Melbourne. Despite high construction costs, two new hotels opened in Sydney in early 2024 boosting new supply.

While international arrivals in March 2024 were down 9% from pre-pandemic levels, the relatively low Australian dollar has seen the average stay for international visitors increasing significantly.

## Renewable Energy and Carbon markets

The Budget created a \$22.7 billion 'Future Made in Australia' (**FMA**) package that includes significant investment in renewable hydrogen, critical mineral processing, clean energy manufacturing, green metals and low-carbon liquid fuels.

### *Renewable Hydrogen and Low-Carbon Liquid Fuels*

The Federal Government will invest \$8 billion from 2024 to 2034 (and \$1.2 billion per year from 2034 to 2040) to support the production of renewable hydrogen. In addition, the Budget allocates \$1.4 million to fast track the initial phase of the Guarantee of Origin Scheme for green hydrogen and bring forward work on green metals, including iron, steel and aluminium.

A further \$20.9 million has been allocated to incentives to support the production of, and demand for, low-carbon liquid fuels (**LCLFs**). This funding will also support development of a LCLF certification scheme through the Guarantee of Origin Scheme.

### *Critical Minerals*

The Federal Government has granted \$566.1 million to Geosciences Australia to explore and create detailed maps of critical mineral deposits under Australia's soil and seabed.

The Federal Government has also committed \$7.1 billion over the next 11 years to support the refining and processing of critical minerals in Australia.

### *Clean Energy Manufacturing*

The Federal Government will invest \$1.4 billion from 2024 to 2035 to support manufacturing of clean energy technologies, especially solar and battery manufacturing capabilities.

A further \$18.1 million has been allocated to foundational initiatives that will support the emergence of Australia's green metals industry. The funding aims to support the production of green iron, steel, alumina and aluminium.

### *Innovation and Renewable Energy Technologies*

The Federal Government will invest \$1.7 billion in the Future Made in Australia Innovation Fund (**Fund**), to be administered by the Australian Renewable Energy Agency (**ARENA**). The Fund will support innovation, commercialisation, pilot and demonstration projects and early-stage development in priority sectors. Fund priority sectors include renewable hydrogen, green metals, low-carbon liquid fuels and clean energy technology manufacturing such as batteries.

In addition, the Federal Government will invest \$1.5 billion from 2027 to 2034 to supercharge ARENA's core investments in renewable energy technologies. This funding will be allocated toward development, demonstration, commercialisation, manufacturing and deployment opportunities to make Australia a renewable energy superpower.

### *Clean Energy Workforce*

The Federal Government has committed \$218.4 million to support the development of a skilled and diverse clean energy workforce in Australia.

The Federal Government has also committed \$134.2 million to ensure workers impacted by the net zero transition are supported during the transition.

*(Continued on the next page)*





### *Regulatory Reforms for Investment, Sustainable Finance, and Approvals*

The Federal Government has committed significant funds to deliver regulatory reforms in key areas to create a competitive business environment in Australia to better attract and deploy investment. The regulatory reforms will facilitate and accelerate renewable energy investments.

The reforms will be introduced as part of the *Future Made in Australia Act* tabled in Parliament this week.

#### *Carbon*

In addition to the measures noted above, the Budget included the following measures specific to Carbon markets and decarbonisation:

- **ACCUs:** an additional \$48.0 million over four years from 2024–25 to implement further reforms to the Australian Carbon Credit Unit (**ACCU**) scheme as part of the Government's response to the Independent Review of Australian Carbon Credit Unit. These reforms will establish the Carbon Abatement Integrity Committee to oversee the new proponent led method development process and strengthen integrity, provide enhanced transparency measures, and support First Nations participation including in supporting consent processes for projects on Native Title land.
- **Safeguard Mechanism & Paris Agreement:** initiatives to increase the supply of ACCUs in connection with the Safeguard Mechanism and \$32.6 million over four years from 2024–25 to establish regulatory frameworks and bilateral instruments to better support heavy industry to reduce emissions to meet Paris Agreement commitments, both in Australia and overseas were also announced.

### **Tranche 2 Anti-money laundering reforms**

The Australian Government will invest \$166.4 million from this year's Budget to support long anticipated reforms to Australia's anti-money laundering and counter-terrorism financing (**AML/CTF**) regime.

The proposed reforms are known as 'Tranche 2' reforms and extend the existing AML/CTF legislation to certain high-risk services including lawyers, accountants and real estate professionals. Australia is currently one of only five countries yet to implement 'Tranche 2' reforms and is at risk of being grey listed by the Financial Action Taskforce (**FATF**). It is likely these reforms will be reflected in legislation by 2026–2027 as this is when Australia's AML/CTF regime will next be assessed by the FATF.

Entities considering investing in Australia should be aware of the proposed reforms and how this may impact their engagement with services providers such as lawyers, accountants and real estate agents who may help facilitate these investments. In particular, the reforms are likely to impose new obligations on high-risk service providers (similar to the obligations that apply to entities already the subject of the AML/CTF regime, such as banks), including compulsory reporting of certain transactions and suspicious activity (known as suspicious transaction or activity reporting in other jurisdictions), implementation and maintenance of an AML/CTF program, and customer due diligence (or 'KYC').

Foreign investors should also bear in mind AUSTRAC's dual role as Australia's AML/CTF regulator and financial intelligence unit. As a financial intelligence unit, AUSTRAC currently collects and analyses financial reports and information from over 17,000 entities to generate financial intelligence that is shared with local and international law enforcement, regulators and national security investigations. As a regulator, AUSTRAC has been very aggressive in its pursuit of regulated entities and has secured record-breaking penalties for AML/CTF failings.



## Key changes for foreign resident CGT regime

The Government intends to broaden the scope of the existing capital gains tax (**CGT**) regime for foreign residents.

Currently, the foreign resident CGT regime applies to assets that constitute “taxable Australian property” (**TAP**) at the time that the non-resident disposes of the relevant asset. TAP includes:

- Australian real property assets, including Australian land, mining rights and leases;
- assets that are used in carrying on a business through a fixed place in Australia;
- shares in a company, or units in a trust, where certain statutory tests are satisfied; and
- options or rights to acquire one of the above assets.

The first proposed amendment will expand the scope of the assets that constitute TAP to include ‘assets with a close economic connection to Australian land’.

The Government is yet to release guidance on the scope of assets that will be included in the expanded definition of TAP and have indicated that they intend to consult on the implementation details of this measure later this year. There are suggestions that this definition may extend to assets such as water rights and certain renewable assets, and we expect more details to be forthcoming once the consultation process commences.

The second proposed amendment is a technical change to one of the tests applied to whether shares or units will be subject to foreign resident CGT. Currently the “principal assets test” requires that the value of the relevant company be principally attributed to Australian real property at the time of disposal. The change will introduce a new averaging rule to apply the principal asset test over a year, rather than at a point in time.

The third proposed amendment is that a foreign resident will now be required to provide a compulsory notification to the ATO if the transaction relates to a sale of shares or units that have a value of more than \$20 million. This notification must be undertaken before the transaction occurs. The existing regime allows foreign residents to provide self-assessed declarations that their shares are not TAP. Whilst little detail is currently known on how compulsory notification will be implemented, foreign resident vendors may need to consider this ATO notification requirement in the context of the broader transaction timeline to ensure any ATO queries are satisfied as required prior completion of the transaction.

The changes to the foreign resident CGT regime will commence on or after 1 July 2025.

These measures are in addition to the 2023-24 Mid-Year Economic and Fiscal Outlook announcement which will apply from 1 January 2025. These measures will increase the foreign resident CGT withholding rate from 12.5% to 15% and reduce the withholding threshold down from \$750,000 to \$0.



# Contributors



## Justin Fox - Corporate

justin.fox@hamiltonlocke.com.au  
T +61 417 220 275

[View Profile](#)



## James Delesclefs – Corporate

james.delesclefs@hamiltonlocke.com.au  
+61 412 034 116

[View Profile](#)



## Alistair Newton – Competition & Consumer

alistair.newton@hamiltonlocke.com.au  
+61 450 922 876

[View Profile](#)



## Clementyne Rawlyk – Foreign Investment

clementyne.rawlyk@hamiltonlocke.com.au  
+61 412 034 116

[View Profile](#)



## Sarah Roettgers – Real Estate

sarah.roettgers@hamiltonlocke.com.au  
+61 438 727 382

[View Profile](#)



## Jessica Smith – Financial Services

jessica.smith@hamiltonlocke.com.au  
+61 448 318 480

[View Profile](#)



## Seema Sandhu – Tax

seema.sandhu@hamiltonlocke.com.au  
+61 2 8072 8271

[View Profile](#)



## Anish Prakash – Tax

anish.prakash@hamiltonlocke.com.au  
+61 488 246 628

[View Profile](#)



## Matt Baumgurtel - New Energy

jmatt.baumgurtel@hamiltonlocke.com.au  
T +61 459 900 080

[View Profile](#)



## David O'Carroll – New Energy

david.ocarroll@hamiltonlocke.com.au  
+61 421 497 311

[View Profile](#)



## Tim Grave – Litigation

tim.grave@hamiltonlocke.com.au  
+61 409 664 118

[View Profile](#)

## SYDNEY

Australia Square  
Level 42, 264 George Street  
Sydney NSW 2000

## MELBOURNE

Level 33  
360 Collins Street  
Melbourne VIC 3000

## NEWCASTLE

Level 3  
21 Bolton Street  
Newcastle NSW 2300

## PERTH

Level 48  
152-158 St Georges Terrace  
Perth WA 6000

## BRISBANE

Level 19  
123 Eagle Street  
Brisbane QLD 4000

## AUCKLAND

Vero Centre  
Level 35, 48 Shortland Street  
Auckland 1010 New Zealand

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