

Australian Investment in Australian Broadcast Media Submission

Executive Summary:

Enabling all Australians to invest in Australian Media

Many Australian investors are restricted in their ability to invest in Australian broadcast media.

Many investors may not even realise that their superannuation, retirement and portfolio investments may be prevented from investing in Australian media because their fund manager is considered foreign-owned.

An unfortunate by-product of the foreign investment laws for media in Australia is that foreign ownership restrictions apply as tightly to Australian funds invested by foreign-controlled Australian fund managers as they do to foreign investors.

These restrictions significantly limit Australian investors' choice of fund managers with exposure to the Australian media sector. This limitation is increasing as the deregulation of the fund management sector is resulting in fewer Australian-owned institutions.

However, all investors suffer from these limitations, irrespective of their choice of fund manager, because the depth of the market for shares in media companies is reduced and uncertainty for investors is increased.

The serious anomalies arising from the current restrictions include:

- Foreign investment in an Australian fund manager can result in the fund manager becoming designated as foreign-owned. Such foreign investment can occur as a result of privatisations and public offerings by fund managers, as well as takeovers and acquisitions. This can trigger divestiture of Australian media assets to comply with the foreign ownership provisions, without any change in the underlying beneficial ownership of Australian investors in these assets.
- The depth of the market for shares in Australian media companies is adversely affected by the lack of qualifying Australian fund managers and the potential for market overhang in media company shares as a result of forced divestitures. This impacts all Australian investors due to effects on share prices and liquidity and inhibits the growth of capital markets for Australian media companies.
- In an environment where competition for capital is as strong as ever, Australian broadcast media companies are placed at a significant disadvantage compared with other Australian industries where Australians are not restricted in their ability to invest.
- In some cases, the superannuation and investment funds of Australian citizens are more easily invested in overseas media companies than they would be in Australian media.

The commercial free-to-air television industry proposes legislative change to resolve these anomalies and enable all Australians to invest in our broadcast media. The

recommendations are based on similar legislation introduced to enable Australian investment in Telstra, Australian airports and Qantas.

These changes will promote more Australian investment in Australian broadcast media for passive portfolio investors. FACTS' members have made individual submissions to the Commission on foreign ownership and control rules. This submission is made against the possibility that the Commission may (for whatever reason) recommend that the foreign ownership and control rules remain intact.

Foreign Investment Limits and their Application to Investment Funds

Australia has clear national controls limiting foreign investment in free-to-air broadcasting licences. Foreign investment in companies holding commercial television licences is limited to a total of 20%, with a maximum individual foreign ownership of 15%.

As well as applying to foreign persons and foreign corporations, the provisions restricting investment apply to investments on behalf of Australian persons by foreign-controlled institutions.

As a result, Australian fund managers, where controlled by a foreign-domiciled company, are restricted from investing in Australia's major broadcasting companies, despite the fact that many of these funds invest large proportions of the investment funds of Australian citizens.

Appendix 1 summarises the existing foreign ownership provisions.

Consequences for Australian investors

The current restrictions mean that Australian investors with portfolio investments managed by foreign-owned fund managers - and there are many such people - are unable to gain exposure to the Australian broadcasting sector through their investment funds. This affects both Australian retail investors with managed investments and industry-based superannuation funds, which Australians are increasingly reliant on for their retirement savings.

Furthermore, a number of anomalies arising from the current foreign ownership provisions result in market uncertainties and inefficiencies which impact on all Australian investors, not only those with portfolio investments managed by foreign-owned institutions.

These anomalies largely hinge on the potential for forced divestment of shares in listed media companies beneficially owned by Australians as a consequence of various transactions triggering the foreign ownership provisions. This can occur in a number of circumstances:-

- Changes in the ownership structure of Australian fund managers can result in these managers becoming designated as foreigners for the purposes of the foreign ownership provisions. This can occur as a result of privatisations and public offerings, takeovers and acquisitions and restructures. Given the tracing provisions in the legislation, it can also be triggered by changes in the ownership structure "upstream" from the fund manager. Again, if the change in status of these fund managers results in the foreign ownership ceiling of any companies being exceeded, forced divestiture of these investments may occur.
- Australian superannuation and investment funds which are not pooled funds may change from an Australian fund manager to a foreign-owned fund manager domiciled in Australia. If this results in the level of foreign ownership in any Australian media company exceeding the 20% aggregate foreign investment ceiling, the fund would be forced to divest some or all of its shareholdings in those companies. This would occur despite no additional foreign capital being invested in the fund or the media company, and no change in the underlying beneficial ownership of Australian investors.

Depending on any provisions for divestiture in the relevant companies constituent documents, divestitures by fund managers other than those whose ownership has changed may also be triggered. For example, the last foreign purchaser to join the share register may be forced to divest rather than an earlier Australian investor who became foreign owned. Although such an anomaly results from the particular mechanisms in companies constituent documents, it nonetheless reflects the practical difficulties arising from the current legislation.

In all of these cases, ordinary Australian investors would effectively be forced, albeit indirectly, to sell their beneficial interests in Australian media companies and significantly reduce their exposure to the sector.

Notwithstanding the apparent strength of the equities markets at present, the uncertainties associated with the effects of these anomalies impacts on all investors, irrespective of whether they have an Australian or foreign-controlled fund manager.

This is because the depth of the market for the shares in these media companies is restricted, with consequent impacts on share prices and liquidity. With the risk of various transactions in the funds management sector resulting in divestment, Australian fund managers and other investors are less willing to expose themselves to a significant market overhang should forced sales come on to the market. In addition, the lack of qualifying Australian fund managers to provide greater depth to the market also inhibits price support and liquidity, to the detriment of all Australian retail investors and superannuants.

The specific exemptions from the foreign ownership provisions granted by the government in respect of the partial sales of Telstra and Qantas provided greater depth to the market for the securities in these companies, which were of benefit to these equity raisings and created greater after-market price and liquidity support.

Adding to the uncertainty and market inefficiencies arising from the current legislation, the complexities of the tracing provisions make the level of foreign shareholdings difficult to monitor in practice. This is problematic in an environment where investments are continually traded and ownership in the funds management industry changes frequently. Uncertainty as to the precise level of foreign ownership at any given point in time exacerbates the risk of dislodgment, under the foreign ownership provisions and divestiture provisions in companies constituent documents.

In many respects, it is easier for Australian funds managed by a foreign owned manager to invest in an overseas television broadcaster or media company than an Australian one.

All of these anomalies appear to serve no purpose other than to limit the opportunities for ordinary Australian investors and the Australian media sector.

Impacts on Australian Media Companies

Aside from the significant impacts on Australian investors and superannuants, Australian media companies are placed at a comparative disadvantage, both with other Australian industry sectors which are not restricted in this manner, and with international media companies which can attract Australian investment funds.

Australian media companies are unable to access the equity capital of Australian investors managed by foreign fund managers. With competition for capital stronger than

ever, both locally and globally, the inability to access these equity funds limits the capability of these companies to fund growth, particularly for smaller companies.

Notably, with the advent of converging digital technologies, many media companies are competing against companies in the emerging media sector which are not restricted in their ability to raise growth funding from Australian investors. This disparity has not resulted from a clear policy decision. Rather, it is the unintended consequence of anomalies in the current legislation.

Which Australian media companies do the investment restrictions apply to?

Listed television broadcasting companies which may be affected by this investment restriction include:

- Publishing and Broadcasting Limited
- Prime Television Ltd
- Seven Network Ltd
- South East Telecasters Ltd
- Southern Cross Broadcasting Ltd
- Spencer Gulf Telecasters Limited
- Sunraysia Television Ltd
- Telecasters Australia Ltd
- Ten Network Holdings Ltd

Which Australian funds are restricted when investing in Australian media assets?

Macquarie Bank estimates that at least eight of the top twenty Australian fund managers are considered foreign under the BSA provisions. In addition a further nine of the top twenty Australian fund managers may be affected by the tracing provisions of the BSA.

RANK	INSTITUTION	AUSTRALIAN EQUITIES UNDER MANAGEMENT (\$B)	DOMICILE
1.	AMP	14.1	Australian [#]
2.	Colonial First State	10.7	Australian [#]
3.	Lend Lease	8.6	Australian [#]
4.	Morgan Grenfell	7.9	Foreign
5.	QIC	7.6	Australian
6.	BT	7.3	Foreign
7.	Maple-Brown Abbott	7.2	Australian
8.	Norwich	5.7	Foreign
9.	National Mutual	5.5	Foreign
10.	National Australia	5.3	Australian [#]
11.	Commonwealth Bank	4.8	Australian [#]
12.	Westpac	4.4	Australian [#]
13.	Mercantile Mutual	4.0	Foreign
14.	NRMA	3.1	Australian [*]
15.	Perpetual	2.7	Australian [#]
16.	Salomon Smith Barney	2.7	Foreign
17.	Rothschild	2.7	Foreign
18.	HSBC	2.4	Foreign
19.	Macquarie Bank	2.4	Australian [#]
20.	GIO	2.2	Australian [#]

* May become part "foreign" after listing

May be affected by tracing provisions

Source: Macquarie Bank Limited / Rainmaker

Experience in Other Industry Sectors

There are several examples in other Australian industry sectors where specific limits have been placed on foreign ownership, yet at the same time, specific exemptions enable foreign controlled funds managers to invest Australian funds in these entities.

These include the partial sale of Telstra, the Qantas sale and the sale of Australian airports. Appendix 3 summarises these provisions.

Proposal

It is proposed that investment funds with a majority of Australian funds under management by a foreign-domiciled company be permitted to invest in Australian media without being restricted by virtue of the foreign ownership provisions. This is to address the anomalies in the current legislation, not to create loopholes and other opportunities to circumvent the current provisions.

This can be facilitated through amendment to the BSA with similar provisions to those introduced for Telstra, Qantas and Australian airports:

There should be an exemption for any shares held by foreign owned companies (or foreign interests through companies) which are in their capacity as:

- (a) (1) trustees/managers of a fund; or
- (2) trustee of a statutory fund of a life insurance company which is a substantially Australian fund.

A substantially Australian fund is a fund:

- (A) in which a beneficial interest in less than 40% of the capital and 40% of the income is held by foreign persons.
- (B) in the case of a life insurance company in its administration of a statutory fund, in which not more than 40% of policy holder liabilities are owed to foreign persons.

or

- (b) custodians who do not have a beneficial interest in the relevant shares and do not have a discretionary right to vote the shares.

Anti-avoidance provisions would prevent anyone carrying out a scheme for the sole or dominant purpose of avoiding the foreign ownership restrictions. The Telstra (Dilution of Public Ownership) Act 1996 contains such provisions (see Division 6, Part 2A).

For consistency, changes may also be required to the Treasurer's Guidelines relating to notification provisions of foreign investment in media to reflect the exemption outlined in the BSA amendments.

No changes will be required to the current control tests.

An even simpler alternative proposal could involve the exclusion of individual institutional portfolio holdings of less than a small maximum limit of no greater than 5%, for the application of the foreign ownership provisions generally.

Benefits of the proposal

The opportunity for more Australians to invest in this fast-growing sector will benefit investors and media companies alike.

All Australian investors, regardless of who manages their portfolio investments, will benefit from addressing the current regulatory anomalies and creating a level playing field for the investment of Australian funds in Australian broadcast media.

Australians will no longer be restricted from investing their own funds in Australian media, simply because of their choice of funds manager. Furthermore, no Australians will be effectively forced to divest their underlying beneficial ownership in Australian media companies, simply because their industry superannuation fund changes its manager, or due to ownership changes in the funds management sector.

Investors with foreign-controlled funds will have greater access to a fast-growing industry sector. Investors in Australian-controlled funds will benefit as a result of increased depth of the market brought about by the creation of a level competitive playing field.

The media sector is an exciting investment area, with new technologies promoting innovation and growth in the sector. However, ready access to equity capital is required if the potential of Australia's broadcast media is to be fully realised on the world stage.

Implementation of these proposals will address the current disadvantage of Australian broadcasting companies competing for capital with other Australian industries and against international media companies. Opening up access to the capital of Australian investors and superannuants will create a deeper capital market, which will be beneficial for both existing and emerging media players.

The market itself will operate more efficiently, with reduced uncertainty over share register changes and without the anomalies arising from current arrangements.

There will increased incentives for funds to invest in Australian media, rather than international media, thereby supporting an important technological growth industry for Australia.

No change to BSA foreign control restrictions

Implementation of this proposal will promote the inflow of Australian investor funds while retaining existing foreign control restrictions in the Broadcasting Services Act.

Again, any policy decisions regarding our foreign investment restrictions on media can be left to the Productivity Commission inquiry.

Further information

Tony Branigan
General Manager
FACTS
Tel: 02 9960 2622

Fax: 02 9969 3520

Appendix 1: Foreign Ownership Restrictions

The Broadcasting Services Act 1992 (“BSA”) provides the following limits on foreign investment in Australian broadcasting media in order to ensure continuing Australian control of broadcast media.

Commercial television broadcasting licences:

- A person who has company interests of 15% or more will be regarded as being in a position to exercise control of the licence.
- Individual foreign ownership of company interests (including ownership of shares) must not exceed 15%.
- Total foreign ownership must not exceed 20 per cent of company interests.
- Under tracing provisions of the legislation, where a company interest of more than 15% is maintained through a chain of companies, the person at the beginning of the chain is to be regarded as being in a position to exercise control of the last company in the chain.

Foreign investment in Australian media is also governed by the Foreign Acquisitions and Takeovers Act (Cth) 1975 (“FATA”) and Government foreign investment policy.

Section 26 of FATA requires a foreign person (or an entity in which foreign persons have a substantial interest) to notify the Treasurer of any proposed “agreement by virtue of which [that foreign] person acquires a substantial shareholding” in an Australian financial or trading corporation. This will occur where a foreign person enters into an agreement to acquire a substantial interest, or already holds a substantial interest, and enters into an agreement to acquire further shares.

A person is deemed to hold a substantial interest in a corporation if the person, alone or together with any associate, is in a position to control 15% or more of the voting power in the corporation or holds interests in 15% or more of the issued shares. Two or more persons hold an aggregate substantial interest in a corporation if they are in a position to control 40% or more of the voting power in the corporation or hold interests in 40% or more of the issued shares.

Foreign investment policy also includes prior notification provisions.

Appendix 2: Descriptions of relevant funds

a. Superannuation and managed funds

The funds management industry attracts investment by Australian individuals of superannuation funds under the superannuation guarantee scheme and direct investment in managed funds. Typically, when institutions invest these funds in securities listed on the Australian Stock Exchange Limited (ASX), the institution, as trustee or responsible entity for the fund will obtain an “interest in a share” under FATA as registered owner of the securities. Where the institution is not simply a custodian but is in addition or instead the manager of a fund or trust, it will obtain an “interest in a share” if the management agreement or arrangements entitled it to exercise the right to vote the share or to control the disposal of the share.

b. Insurance funds

Another type of entity that may invest in Australian securities is a statutory fund, within the meaning of the Life Insurance Act 1995, or a life insurance company. Under that Act, the life insurance company will hold both beneficial and legal interest in shares, and hence will have an “interest in a share” under FATA. However, in many cases, a large proportion of policyholder liabilities of the statutory fund will be owed to Australian persons.

c. Custodian

It is also common for institutions to act as custodian of securities where the beneficial interest in those securities is retained by a third party. If the custodian is foreign its holding of the shares as custodian will fall under the provisions of FATA even where the third party with whom the beneficial ownership remains is Australian.

Appendix 3: Legislative Examples

Airports Act (Cth) 1996

The Airports Act limits foreign investment in Australian airports. Sections 40 and 41 provide that an unacceptable foreign ownership situation exists if there is a group of foreign persons who hold, in total, a “stake” in an airport-operator company of more than 49%. In determining whether a person has a “stake” in an airport-operator company, an interest in shares in an airport-operator company will be disregarded if it is “an interest of a prescribed kind in a share, being an interest held by such persons as are prescribed” (clause 9(1)(c) of the schedule to the Airports Act.

Under Regulation 6 of the Airports (Ownership-Interests in Shares) Regulations 1996 a person’s interest in a share is an interest of a prescribed kind if:

- (a) the interest arose solely as a result of an action by the person in that person’s capacity as trustee or manager of an investment fund; and
- (b) the person is a person prescribed under Regulation 7(1)

Investment fund is defined to mean the following:

- (1) a unit trust (but not a discretionary trust);
- (2) a statutory fund of a life insurance company;
- (3) a superannuation entity; or
- (4) an exempt public sector superannuation scheme, within the meaning of the Superannuation Industry (Supervision) Act 1993.

Regulation 7(1) provides that a person is prescribed if the Secretary declares the investment fund of which the person is trustee or manager to be a substantially Australian investment fund. To be eligible to be declared a substantially Australian investment fund the investment fund must be a fund in which a beneficial interest in less than 40% of the capital, and 40% of the income, is held by persons who are foreign persons.

Telstra Corporation Act (Cth) 1991

Under this Act, foreign ownership is limited to a total stake of 11.6667%, and no foreign person may hold a stake of more than 1.6667%.

However, the Telstra Corporation (Ownership – Interests in Shares) Regulations 1997 provide for an exemption to the ownership provisions in the case of the trustee or manager of an investment fund. Regulation 7 provides that an interest in a share is to be disregarded for the purposes of the ownership provisions according to similar provisions as in the Airports Ownership regulations.

Regulation 16(1) provides that a person is prescribed if the investment fund of which they are a trustee or manager is a substantially Australian investment fund. A substantially Australian investment fund means a fund:

- (a) in which a beneficial interest in less than 40% of the capital and 40% of the income for distribution, is held by persons who are foreign; or

(b) in the case of a life insurance company, in its administration of the statutory fund in which not more than 40% of policy holder liabilities of the statutory fund are owed to foreign persons.

The Telstra regulations differ from the Airports regulations in that the exemption applies automatically without the need for an application to be made. In addition, the second limb of Regulation 16(2) recognises the particular nature of statutory funds under the Life Insurance Act.

Qantas Sale Act 1992

Clause 7 of this Act includes the safeguard that foreign persons must not have relevant interests in more than 49%, and individual foreign persons must not have relevant interests in more than 25%, of the aggregate value of the issued share capital of Qantas.

“Australian person” is defined in the QSA to include:
a person in the capacity of a trustee or manager of a fund in which the total interests of Australian persons represents 60% or more of the total interests in the fund.

The rationale behind such a restriction is to ensure that where a majority of moneys in a fund are invested by Australian persons, the fund is not classed as a foreign person just because the person managing the investment of the fund is foreign.

Financial Sector (Shareholdings) Act

The Financial Sector (Shareholdings) Act 1998 imposes restrictions on financial sector companies. Section 10 provides that an unacceptable shareholding situation exists in relation to a particular financial sector company and a person if the person and their associates control more than 15% of the voting power in the company.

Clause 8 of Schedule 1 provides for the regulation of prescribed interests that are to be disregarded. No regulations have yet been issued under this Act.