

IT'S PUBLIC

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CONDITIONALLY YOURS: TACKLING FIRB UNCERTAINTY IN FOREIGN BIDS

How dealmakers can assess or improve a foreign bids' approval prospects.

Tectonic shifts in the global order are seeing security and economic considerations collide. While nations like Australia will proclaim to be 'open for business' and welcoming of foreign investment, actions speak loudly. In pursuit of economic security, foreign direct investment regimes around the world are increasingly imposing higher fences and bigger yards on foreign investment.

For Targets, Bidders and their boards, this elevates a critical question: How to assess or improve a foreign bids' approval prospects? This article looks at recent FIRB deal approval data and analyses prominent deals to provide dealmakers a playbook.

KEY TAKEAWAYS FOR DEALMAKERS



Be strategic

Ensure the application of Australia's foreign investment regime is considered early as part of deal planning and execution.



Assess the risk

Establish frameworks for assessing FIRB risk, applying the "Who, What and How" framework from Australia's Foreign Investment Policy.



Prepare to accept broad conditions

KWM's analysis and FIRB's approach indicates Bidders will likely be required to accept an increasingly broad range of conditions with limited carveouts.



Put your money where your mouth is

With the heightened focus on FIRB risk, expect to see reverse break fees and ticking fees increasingly deployed to address delays in obtaining or a failure to obtain FIRB approvals.

THE FIRB DIMENSIONS OF RISK

Who

In a rapidly shifting geopolitical environment, assessing a foreign bid is not straightforward. Who is considered safe? FIRB is said by pundits to favourably consider investors from the Five Eyes intelligence-sharing arrangement (comprising the USA, UK, Canada and NZ alongside Australia). The Coalition Opposition has suggested a white-list of investors¹ from the Five Eyes with the addition of Japan and India. However, in reality bidders rarely neatly fit within these lists. In any event, as Lord Palmerston keenly observed in 1848, States "have no eternal allies, and ... no perpetual enemies" and a white-list today may be a shade of grey tomorrow.

The good news for Target boards is that there is an effective way to assess this risk. Securing information about the capital stack of the Bidder, any proposed syndications and the Bidder's FIRB history enables ready comparison against FIRB's latest positions.

For Bidders, joining forces with Australian capital can potentially cleanse foreign investment delays or concerns around control, access and influence.

1. The Hon Angus Taylor MP Shadow Treasurer, Keynote address for the AFR Business Summit 2025, Wednesday 5 March 2025

What

Sectors and assets considered sensitive are also growing.

The “small yard, high fence” strategy of protecting economic assets is subject to immense pressure to expand the ‘yard’². When the Security of Critical Infrastructure Act was introduced in 2018 it covered four sectors, namely electricity, gas, water and ports.

By September 2023, the Federal Government had more than doubled the sectors of national significance, adding a further 11 sectors. The latest Quarterly Report on Foreign Investment (1 July 2024 to 30 September 2024) identified that 6% of all commercial foreign investment applications in the quarter related to national security actions.

Sensitive areas likely to remain subject to increased scrutiny by the Federal Government include health, technology and data (including software as a service), technologies and assets to deliver a net zero transition (including renewable energy and critical minerals) and housing.

Recent Government interventions in high-profile distressed businesses, such as Rex and the Whyalla Steelworks, suggest Targets with large Australian workforces are also likely to face heavy scrutiny.

How

Understanding Bidder ownership structure will be critical to any Target assessment. Ensuring that ownership is transparent will be critical to securing timely FIRB approval.

Targets are likely to require Bidders to provide a clear articulation of who will ultimately control the Bidder and therefore the Target once the proposed transaction is implemented.

EVOLVING FIRB CONDITIONS

FIRB commonly imposes conditions on transactions. Typically, these conditions are designed to manage control, influence and access of a Target where the Who, the What or the How raise sensitivity ‘red flags’.

Under the more flexible legislative regime, the Federal Government agencies FIRB consults on matters of national interest are increasingly using the FIRB process to impose conditions. This is resulting in a panoply of conditions relating to governance, security clearances, operational involvement, access to data and property, cybersecurity and data protection and tax.

KWM conducted an analysis of 2024 public deals to provide you a data-driven picture of what this looks like.

We looked at takeover bids and schemes of arrangement which involved an Australian listed target, were announced between 1 January 2024 and 31 December 2024, and had a deal value over A\$25 million.

The results reveal dealmakers are quickly adapting to the regulatory risk.

2024 DEALS

23

out of the 49 (47%)

deals required
FIRB approval

5

of 23 (22%)

were ‘broad formulation’ –
requiring the Bidder to accept
any conditions imposed by FIRB
relating to a particular area – eg
cyber, governance, security or tax,
with limited carve outs.

14

out of 23 (61%)

had a reverse break
fee triggered by
material breach.

3

of the 5

broad formulation
had a reverse break fee triggered
by
material breach.

The findings surface two main issues for dealmakers:

1. The lack of standard conditions as FIRB (and consult agency) practice evolves; and
2. The growing unpredictability regarding conditions which may be imposed.

They raise an important question: how will market practice evolve in response? Expect transaction documents to increasingly rely on a broad brushstroke approach to what FIRB conditions must be accepted by a Bidder, with limited carve outs.

². Address to the United States Studies Centre

REVERSE BREAK FEES AND TICKING FEES

Reverse break fees are increasingly a part of the Australian public M&A landscape.

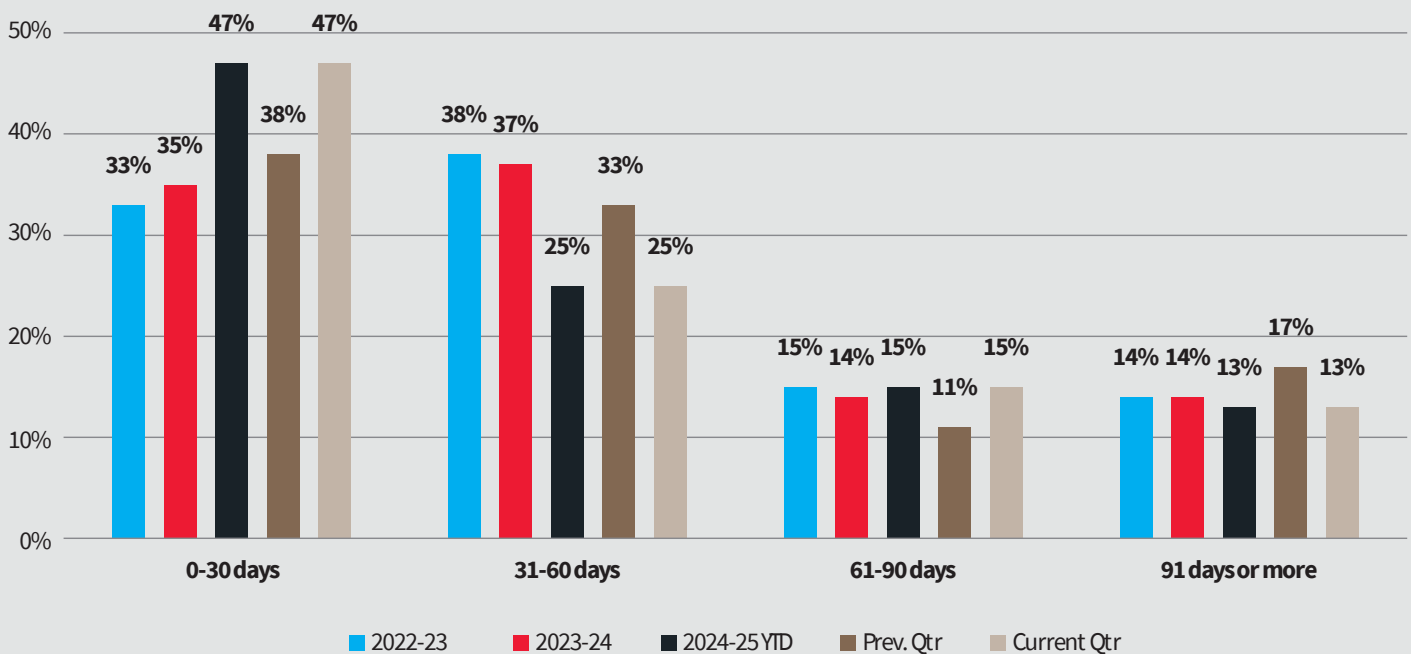
Following the US Executive Order prohibiting Nippon Steel's bid for U.S. Steel³, recent press has suggested US Targets are more likely to demand deal protection, imposing reverse termination fees to protect against a deals' failure for regulatory or political reasons.

In an environment of transactional diplomacy and the associated uncertainty with regulatory intervention, expect reverse break fees to have a greater prominence in Australian transactions in 2025 for a failure by Bidders to accept FIRB approvals on the conditions broadly described.

KWM's analysis of Australian-connected deals announced in 2024 found that 3 of the 5 deals with broad FIRB conditions included a reverse break fee for material breach – effectively a backdoor to a reverse break fee for a failure to obtain FIRB. Interestingly, none included a reverse break fee for failing to obtain FIRB by the end date.

While the latest Quarterly Report on Foreign Investment noted the median processing time for approved commercial investment proposals, the median hides the reality of delay.

APPROVED INVESTMENT PROPOSAL PROCESSING TIMES (BY NUMBER OF DAYS)



Source: Quarterly Report on Foreign Investment – 1 July 2024 to 30 September 2024

During bids where timing for FIRB approvals remains uncertain, ticking fees can encourage shareholder support (particularly in a contested bid) and provide Target boards with comfort. Recent deals show the adoption of this practice: following on from the ticking fee in the Brookfield Origin Scheme, the Saint-Gobain CSR Scheme also included a ticking fee if the scheme did not become effective within four months of signing.

LOOKING AHEAD

This discussion underlines the importance of a transparent and timely approvals regime for both antitrust and foreign investment. The Federal Government promised last year that FIRB processes would be streamlined. We hope this commitment survives the forthcoming election, is delivered this year and maintained. Similarly, it's critical that the Government properly supports and takes accountability for the implementation of the new Australian merger laws. Delay in FIRB, ACCC or other regulatory processes will put deals in jeopardy.

For dealmakers, appreciating the politics and having a clear strategy to proactively manage regulatory risk as part of any deal will be critical in 2025. It is essential that the application of Australia's foreign investment regime is taken into account early as part of deal planning and execution.

3. Order Regarding the Proposed Acquisition of United States Steel Corporation by Nippon Steel Corporation | The White House



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