

The Treasury

Phase 2 Overseas Investment Act Reform Information Release

July 2019

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Chair,

Cabinet Economic Development Committee

Phase two of the Overseas Investment Act reform – Release of Consultation Document

Proposal

1. This paper seeks agreement to release the attached consultation document titled 'Overseas Investment 2005: Facilitating productive investment that supports New Zealanders' wellbeing' ('Consultation Document').
2. Consistent with paragraph 2.39 of the Cabinet Manual, I submit this paper with the knowledge and approval of the Minister of Finance.

Executive Summary

3. In October 2018, Cabinet agreed to commence the second phase of the Overseas Investment Act 2005 (the 'Act') reforms ('Phase Two reform') and release the terms of reference for that reform ('Terms of Reference') [CAB-18-MIN-0481].
4. The Phase Two reform aims to ensure the Act strikes the right balance between:
 - providing a clear pathway for consent for investment that supports a productive, inclusive and sustainable economy, and creating opportunities for regions and businesses to grow and connect internationally;
 - providing appropriate protection against risks to New Zealand associated with the overseas ownership of sensitive assets, with particular consideration of whether New Zealand's national interest is sufficiently protected; and
 - imposing compliance and administrative costs that are proportionate to the risks associated with overseas investment.
5. This paper seeks approval for public release of the Consultation Document, which describes a range of concerns with the Act and seeks feedback on potential options for reform.

Background

6. Open capital markets and beneficial foreign direct investment can offer a number of economic advantages including better access to markets, technology and capital, and, as a result, a more productive economy. However, overseas control of sensitive New Zealand assets can also give rise to a number of risks. It may conflict with New Zealand's national interest, or run contrary to the view held by some that our sensitive assets should be owned and controlled by New Zealanders.
7. The Act is the principal tool for regulating foreign investment into sensitive New Zealand assets. It provides Ministers with a mechanism to screen investments by overseas persons in sensitive land, significant business assets and fisheries quota, and impose conditions on those investments. In the case of investment in sensitive land, it also allows Ministers to prevent an investment if the investor is unable to demonstrate the investment's benefit to New Zealand.
8. There is a perception that the Act is overly complicated and may discourage some productive investment in New Zealand. Conversely, there are concerns about some significant gaps in the Act's coverage – for example, it limits decision makers' ability to consider holistically whether an investment is in New Zealand's national interest.
9. The first phase of reform to the Act, which came into force on 22 October 2018, was the most significant reform of the Act in more than a decade ('Phase One reform'). It included a restriction on foreign buyers of existing residential homes and rationalised the regime for forestry investment by requiring consent for acquisitions of forestry registration rights and certain other profits-à-prendre.
10. The Phase Two reform is one of the Government's initiatives under the 'Grow and share more fairly New Zealand's prosperity' priority outcome, supporting the development of a productive, sustainable and inclusive economy.
11. The Terms of Reference indicated that there would be a public consultation process and that changes would be enacted during this parliamentary term. This is an ambitious timeframe, and any delays during the policy development and legislative process could compromise the Government's ability to deliver the reform by mid-2020.
12. Since release of the Terms of Reference, Treasury officials have conducted targeted consultation on the operation of the Act. This consultation has informed the preparation of the Consultation Document.

Consultation Document – approach

13. Public consultation and engagement is critical to the success of the Phase Two reform. This is a significant opportunity to improve the Act and input from stakeholders, including investors, Māori and the wider public, will be important to ensure the reform process is well informed.
14. In preparing the consultation materials, officials have been mindful of the competing needs for the consultation to be accessible to a non-specialist audience and detailed

enough to be meaningful to a specialist audience. Officials have taken the following steps to ensure that these two needs are both met:

- The Consultation Document contains sufficient detail to ensure that specialist audiences, and others wishing to engage in the technical details of the reform will be able to do so.
 - A shorter, more accessible, summary of the issues and options under consideration has also been prepared to assist those who do not wish to engage in the technical detail. A draft is attached to this Cabinet paper for your information.
 - Officials intend to hold separate town hall style discussions for specialists and non-specialists, and regional hui, with materials tailored for each audience.
 - An external editor has reviewed all of the consultation materials to ensure readability.
15. The Consultation Document's purpose is to test the Government's understanding of problems with the Act and the feasibility of options for reform. The Consultation Document does not contain any preferred options, however impact tables do compare some options. Following consultation and further analysis of options, I will form views on preferred options for reform to present to Cabinet for its consideration.

Consultation Document - structure and content

16. The document is split into four parts. The first part provides context about overseas investment in New Zealand and an overview of the Act, the next three parts consider issues and options relating to:
- who is subject to screening under the Act;
 - what assets are screened; and
 - how the screening process works.
17. The Consultation Document does not cover:
- [2]
 - detailed technical issues with the current regime, which will need to be resolved as part of the Phase Two reform.

I still intend to consider these issues. Their exclusion from the Consultation Document does not preclude them from being addressed as part of the Phase Two reform.

Context

18. The core tension that runs through the Act is that New Zealand needs productive overseas investment but there is inherent value in New Zealand ownership of certain assets, and overseas control of those assets gives rise to some risks. The purpose of the reform is to consider whether the correct balance has been struck so that the Act operates as efficiently and effectively as possible, while ensuring appropriate provision is made to protect New Zealand interests.

What we screen

19. There is an opportunity to better identify the types of land and interests that are subject to screening, particularly in respect of land adjoining sensitive land in commercially-zoned areas. Stakeholders (retirement villages, for example) have expressed concern that the Act defines sensitive land too widely in that respect and thereby imposes unnecessary compliance costs. This section of the document also discusses the treatment of leasehold interests in land. It does not contain options to remove the screening requirements from our most sensitive land, such as farmland, foreshore, and seabed.

Who we screen

20. There is an opportunity both to reduce the number of entities required to obtain consent to acquire sensitive New Zealand assets, as well as to reduce the number of transactions that require consent. This section discusses opportunities to address concerns:
 - that the current definition of an ‘overseas person’ seems overly broad and therefore imposes disproportionate compliance costs on those investors that present a low risk to New Zealand. In particular, it captures a range of companies that are, by any other measure, fundamentally New Zealand companies; and
 - about the extent to which the Act should screen small acquisitions or changes in shareholdings by overseas persons, or passive shareholdings where the overseas person exercises no control over the sensitive asset.

How we screen

21. There is an opportunity to improve how we screen overseas investments. Existing requirements are complex, costly and limit government’s ability to consider the full impact of investments. This section discusses:
 - options for improving the investor test;
 - options for improving the benefit to New Zealand test, including whether it should allow consideration of additional factors;
 - whether New Zealand should introduce a ‘national interest’ test or another test that would allow a more holistic assessment of an investment’s likely effects – and how this test might interact with the benefit to New Zealand test;

- the requirement to offer certain types of land to the Crown;
- the requirement to publicly advertise farmland; and
- whether there is scope to improve decision-making timeliness.

Enhanced national security screening

22. The *How we screen* section also seeks feedback on an option to screen transactions not currently subject to the Act (for example, investments in business assets worth less than \$100 million), where these present potential risks to national security. Coupled with a national interest test applied to transactions already subject to the Act, this would significantly strengthen government's ability to manage national security risks of overseas investment.

23. This would be a significant addition to the Act and an expansion of its scope. ^[4]

24. [Legally privileged (paragraphs 24 and 25)] ^[6]

25.

26. This power would be targeted at smaller transactions. By definition it is therefore more likely to capture smaller firms, possibly in the high-tech sector, that were previously not captured by the investment screening regime.

27. Such a power would not be unique internationally. For example:
- The Canadian government has the capacity to deny consent to any investment by an overseas person in a new or existing Canadian business if it is likely to be detrimental to Canada’s national security.
 - The Committee on Foreign Investment in the United States can block, modify, or unwind any transaction by or with any foreign person that could result in foreign control of a United States’ business.
28. Given the early stage of policy development, the Consultation Document provides less detail on the design options for this proposal than other components of the reform. Instead, the document seeks feedback on the key design choices that will be required, for example, what type of notification process is appropriate, and which agency would operate this new function.

Next steps

29. There will be around five weeks for consultation following the public release of the Consultation Document. This timeframe is short but necessarily so to ensure that we may enact the reform this parliamentary term. To facilitate engagement, officials will hold public meetings and hui around New Zealand to meet with stakeholders, including Māori, so that all interests are heard.
30. [4]
31. A timeframe showing key milestones in the Phase Two reform is set out below.



Consultation

32. The Treasury prepared this Cabinet paper and the attached Consultation Document. The following agencies were consulted: Department of the Prime Minister and Cabinet (National Security Group), Ministry of Foreign Affairs and Trade, Land Information New Zealand (including the Overseas Investment Office), Ministry of Business, Innovation and Employment, Ministry of Housing and Urban Development, New Zealand Trade and Enterprise, Te Puni Kōkiri, Ministry for the Environment,

Ministry for Primary Industries, Ministry of Justice, Department of Conservation, Ministry for Culture and Heritage, Inland Revenue, Te Arawhiti, Heritage New Zealand, and Crown Law.

33. The Department of the Prime Minister and Cabinet (Policy Advisory Group) has been informed.

International Obligations [legally privileged]

34. ^[6]

- 35.

Financial Implications

36. This paper has no direct fiscal implications.
37. There will be financial implications associated with any policy changes arising from the Phase Two reform. The scale of these costs and affected agencies (likely to include Land Information New Zealand as well as New Zealand's security agencies) will be dependent on the changes that are agreed to by Cabinet. These may include implementation costs, costs or savings associated with the processing of applications, and the monitoring and enforcement of consents. Future decisions will be required as to whether costs should be Crown funded, recovered from fee payers or a mixture of both.
38. The sequencing and magnitude of the changes arising from the Phase Two reform may mean that the timing of the upcoming review of the interim fees agreed to in the Phase One reform may need to be delayed if changes are proposed to the application process and evidential tests associated with the interim fees.
39. Greater detail regarding potential financial implications will be provided in future Cabinet papers when policy decisions are sought.

Human Rights

40. There may be human rights implications arising from this paper. The Act, and therefore reforms to the Act, treats people differently depending on their national origins, which triggers consideration of the right to freedom from discrimination (on the grounds of national origin) under the New Zealand Bill of Rights Act 1990.

Further work will need to be done to assess whether any reform is consistent with the New Zealand Bill of Rights Act 1990.

Legislative Implications

41. There are no legislative implications arising directly from this paper.

Regulatory Impact Analysis

42. Regulatory impact analysis is not required at this stage. The Consultation Document incorporates elements of regulatory impact analysis. A regulatory impact statement will be prepared when policy decisions are sought.

Publicity

43. The Consultation Document will be made available on the Treasury website. I will issue a media release when the Consultation Document is released. A programme of stakeholder engagement is planned to follow the release.
44. The Consultation Document seeks feedback on whether the overseas investment regime should include: consideration of Māori cultural values and water extraction in the benefits test, and a national security element. Each of these topics (along with overseas investment, generally) will likely attract public interest. The Consultation Document will also likely attract international interest, from overseas governments and investors.

Pro-active Release

45. I intend to publish this Cabinet paper and the Consultation Document online within 30 business days of Cabinet making the decisions required by this paper as required by Cabinet Office circular CO(18)4, subject to redactions as appropriate under the Official Information Act 1982.
46. ^[1]

- Legally privileged information.

Recommendations

47. I recommend the Committee:
1. **note** that the purpose of the Phase Two reform is to ensure that the Act strikes the right balance between facilitating beneficial investment in New Zealand while ensuring that Ministers have flexibility to prevent investment that is not in New Zealand's national interest.

2. **note** that the consultation is seeking views on the options set out in the Consultation Document, allows for the public to raise additional options and does not express any view on preferred options.
3. **note** that the Consultation Document seeks feedback on options for:
 - *What we screen*: better identifying the sensitive assets and types of interest in those assets that needs to be screened;
 - *Who we screen and when*: reducing the number of entities required to obtain consent to acquire sensitive New Zealand assets (for example, listed retirement villages acquiring residential land), as well as opportunities to reduce the number of transactions that require consent;
 - *How we screen*: improving how we screen overseas investment, as existing requirements are complex, costly and limit government's ability to consider the full impact of investments.
4. **agree** that the Associate Minister of Finance release the attached Consultation Document to the public.
5. **authorise** the Associate Minister of Finance to approve minor amendments and refinements to the Consultation Document prior to its public release.
6. **note** that the public consultation period is intended to commence from 18 April 2019 and conclude on 24 May 2019.
7. ^[4]
8. **note** that there will be financial implications associated with any policy changes arising from the Phase Two reform.

Authorised for lodgement

Hon David Parker
Associate Minister of Finance