The Treasury

Overseas Investment Act 2005: Phase Two Reform Package Information Release

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[33]	9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
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Office of the Associate Minister of Finance (Hon David Parker)

Chair,

Cabinet Economic Development Committee

Overseas Investment Act phase two reform: Package of reform

Proposal

1. This paper seeks agreement to policy decisions on the design of the reform package for the phase two reform ('Phase Two reform') of the Overseas Investment Act 2005 ('the Act').

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. New Zealand needs productive overseas investment. Advantages include better access to markets, technology and capital, and, as a result, a more productive economy. However overseas control or ownership of sensitive assets can result in some risk, and can run contrary to the view that there is inherent value in New Zealand ownership of our most sensitive assets.

4. Our overseas investment regime must balance these competing tensions by ensuring that New Zealand has access to the investment we need while also ensuring the government has the tools to manage risks associated with that investment.

5. There is a lot of evidence that the regime does not have this balance right. We screen many transactions where there is either little to no risk, or the amount of risk is disproportionate to the time and cost of screening. The regime also has some clear gaps. In particular, there is almost no ability to consider risks to national security and public order, which is unique among comparable regimes in other countries.

6. I propose to reform the regime so that it better strikes that balance by:

6.1. Ensuring the regime manages risk: improving the Government's ability to manage investment in our most sensitive and high risk assets, and

6.2. *Cutting unnecessary red tape:* simplifying the decision-making process and removing transactions from the regime where screening is not needed to manage risk.

7. [1]

[31]

Instead, I propose a range of improvements to the special land provisions and seek Cabinet's direction on whether the offer back should be mandatory or voluntary. The law is currently ambiguous on this point.

8. I consider that my proposals strike the right balance and send a message that New Zealand is open to productive foreign investment. However, there is a risk that the agri-business community may view them as tightening the regime given my proposal to embed the current rural land directive in primary legislation and the option of considering any likely or actual environmental harms as part of the consent process for the purchase of non-urban land of greater than five hectares.

Background

9. Overseas investment can bring a range of benefits, including job creation, new technologies, increased human capital, and more diverse international connections, including access to global distribution networks and markets.

10. However, overseas investment can also pose risks. Overseas investment can take ownership and control of economic activity out of New Zealand and high levels of foreign ownership of sensitive New Zealand assets can conflict with a view that New Zealanders[1] should own or control those assets. [1]

11. The Act is New Zealand's principal tool for regulating foreign investment in sensitive New Zealand assets.[2] It is not, however, the only or best tool for regulating foreign investors' conduct (other than ensuring conditions imposed on a consent are complied with). Overseas persons operating in New Zealand are – like domestic investors – subject to our laws governing their activities, including those related to tax, land use, environmental protection and criminal activity.

12. The Act seeks to balance the need to support high-quality investment and ensure that the government has tools to manage any risks. It does so by providing an enduring framework for screening foreign investments in sensitive land, significant business assets (generally assets worth at least $100 million), and fishing quota to help ensure that they benefit New Zealand. However, there is a lot of evidence to suggest that we do not have the balance right.

13. The Act requires a range of low-risk investments and investors to get consent, and the consenting framework is complex and does not always target the right people. This

1 New Zealand citizens and residents that spend a majority of their time in New Zealand.

2 By some measures, 15% of foreign investment into New Zealand is covered by the Act.

unnecessary red tape increases costs and contributes to our poor performance in attracting foreign investment relative to other small advanced economies. This reduces New Zealand's productivity growth, and consequently opportunities to improve living standards deliver on our economic strategy. Improving access to deeper pools of high quality capital is vital if we are to ensure that New Zealand firms can innovate and grow (as identified by the Government's Economic Plan dated September 2019).

14. While the regime overreaches in many areas, it also has clear gaps. Unique among comparable regimes, there is almost no capacity to consider an investment's implications for New Zealand's national security or public order. There is also limited ability to decline investments that are not in our national interest, or further restrict investment in our most sensitive assets. As markets become more global [1] we must reconsider this position.

How the screening regime works

15. The Act requires overseas persons[3] to get consent before acquiring sensitive land,[4] significant business assets or fishing quota. This requirement reflects the Act's purpose: that it is a privilege for overseas persons to own sensitive New Zealand assets.

16. The test that the overseas person must satisfy to obtain consent depends on the type of sensitive asset being acquired. If:

16.1. *Significant business assets* are being acquired, the overseas person must only satisfy the investor test, which focuses on the characteristics of the overseas person.

16.2. *Sensitive land* is being acquired, the overseas person must satisfy the investor test and the benefits test, which requires the overseas person to deliver certain benefits to New Zealand, unless:

16.2.1. *Residential land* is being acquired, then there are a number of tests that largely focus on the land's use. For example, a person with a residence class visa can get consent to acquire residential land (that is not sensitive for any reasons other than it being residential) if they commit to becoming a tax resident, spending the majority of each year in New Zealand, and using the property as their primary residence, or

16.2.2. *Forestry activities* will occur on the sensitive land, then the overseas person must satisfy the investor test and one of two streamlined benefits tests or the general benefits test.

3 Broadly speaking, non-New Zealand citizens and resident, and bodies corporate, trusts and other unincorporated entities that are 25% or more owned or controlled by overseas persons.

4 This includes non-urban land over five hectares, residential land and lifestyle land, and land adjoining sensitive areas such as the foreshore.

16.3. *Fishing quota* is being acquired, the overseas person must satisfy the investor test and a national interest test that is similar to the benefits test but has some elements specific to fisheries.

17. The Overseas Investment Office ('OIO') is the Act's regulator. It makes decisions on some applications and advises decision-making Ministers on others.

Previous reform

Phase One

18. 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'). It placed restrictions on overseas persons buying existing residential homes, and streamlined and rationalised the regime for forestry investment by requiring consent for acquisitions of forestry registration rights and certain other profits-à-prendre.[5]

19. A review of the Phase One changes to the treatment of forestry will commence no later than 22 October 2020.[6]

Overseas Investment Office procedural review

20. The OIO is undertaking a programme of continuous improvement to reduce the length and overall cost of the application process to applicants. In 2018, two external reviews found that the changes had increased the quality of applications, and reduced screening time. Many of the remaining problems with the regime are driven by legislative and regulatory requirements which the OIO and applicants must follow. My proposals aim to address these issues so the OIO is better able to operate in an effective manner, whilst encouraging further operational improvements across the regime.

Aim of the Phase Two reform

21. 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.

22. Cabinet agreed to commence the reform and released the Terms of Reference in October 2018 (CAB-18-MIN-0481).

23. If adopted, the Phase Two reform will be the first comprehensive set of changes to the Act since 2005. The aim of the reform is to better achieve the balance between attracting productive overseas investment while also managing the risks associated with overseas investment by:

23.1. enabling the government to effectively manage overseas investment, while

5 A profit a prendre is a right to take from another person's land something that is part of the soil or is on the soil and is the property of the landowner.

6 This is consistent with the requirements of section 10 of Part 1 of Schedule 1AA of the Act.

23.2. ensuring that the Act operates efficiently and effectively, and

23.3. supporting overseas investment in productive assets.

24. The Phase Two reform does not revisit substantive issues addressed in Phase One (for example, requiring screening of purchases of residential land and forestry rights over sensitive land by overseas persons).

25. The Terms of Reference indicated that legislative changes would be enacted during this parliamentary term. This is an ambitious timeframe, [34]

Public consultation showed divergent views of the Act, but that reform was necessary

26. A public consultation document was released in April (DEV-19-MIN-0078). This document included options for altering who is subject to the Act, what assets require screening and how the screening process works.

27. During May 2019, officials held meetings with stakeholders and the public (19 meetings with approximately 175 attendees throughout New Zealand and in Sydney). This included meetings open to the public, hui with representatives from iwi organisations and Māori businesses and meetings with technical audiences and investors. 733 written submissions were also received.

28. Consultation highlighted the competing tensions that the Act must balance. Stakeholders underscored the extent of the Act's problems in terms of time and cost. Many of the Act's users noted that applying for consent routinely costs more than $100,000 (excluding fees charged by the regulator) and that decision-making times are much longer than in other jurisdictions, which was discouraging investment in New Zealand.

29. Conversely, stakeholders also expressed concerns that the Act does not:

29.1. allow decision-makers to assess whether proposed investments are in the overall national interest, or

29.2. reflect important underlying values, particularly in relation to water and environmental sustainability more broadly.

30. Māori stakeholders were also generally keen to see more engagement with iwi and hapū, to ensure decisions take appropriate account of the impacts on Māori.

31. The consultation document did not include proposals to:

31.1. legislate the higher bar this Government has introduced for overseas persons' purchases of rural land. This proposal does not amount to a change to current policy but elevates it from a direction, embedding it in the Act. Future

governments wanting to dilute current settings will have to amend the Act, rather than change this by Ministerial directive, or

31.2. enhance the regulator's enforcement powers, [4]

Reform is required to improve the government's ability to manage high-risk investment and simplify the decision-making process

32. My proposals for reforming the Act will build on the changes in Phase One and aim to address many of stakeholders' concerns by:

32.1. ***Ensuring the regime effectively manages risks*** – improving the government's ability to manage investment in our most sensitive or high-risk assets, which will maintain the social licence for trade and investment, and

32.2. ***Cutting unnecessary red tape*** – facilitating the high quality and productive investment New Zealand needs by simplifying the decision-making process and removing transactions from the regime where screening does not substantially improve the government's ability to manage risks associated with the investment.

33. There is a risk that placing further restrictions on foreign investment – particularly the proposal to embed restrictions on acquisitions of farmland into the Act, [1]

will overshadow proposals to cut red tape. I consider that on balance my proposals will send a signal that New Zealand is open to the type of productive foreign investment we need.

Ensuring the regime effectively manages risks

34. In Phase One, this Government introduced restrictions on foreign buyers of residential homes, addressing a key gap in the regime. Though the Act is complex and expansive in scope, a number of gaps remain. In particular, the Act does not:

34.1. set a high enough bar for investments in our farmland

34.2. sufficiently give decision-makers the ability to decline investments that are ordinarily screened if they are not in our national interest (including security interests)

34.3. allow screening of certain other strategically important investments to consider whether they pose risks to New Zealand's national security or public order, or

34.4. provide the regulator with sufficient enforcement tools to deter non-compliance.

35. My proposals address these gaps thereby reducing the possibility of investment that might negatively affect New Zealand in the short and long term.

More enduring protection for our farmland

36. Farmland has a special importance to New Zealand. It has significant economic and cultural value. It is central to our economy, and our farmers are among the world's most capable. This means it is a special privilege for overseas persons to own or control farmland, and the case for overseas investment in this farmland is less compelling.

37. In 2017, we issued the Ministerial directive letter, which included a rural land directive raising the bar for overseas investments in rural land (all non-urban land over five hectares, excluding forestry land). It means that overseas persons must deliver increased benefits – with a genuine point of difference from what a New Zealander could or would do – to earn the special privilege of owning our rural land.

38. I propose enshrining the rural land directive in legislation to ensure that future governments are accountable to Parliament for any changes to this Government's policy. Overseas persons seeking to invest in farmland will have to deliver benefits with a substantial point of difference – such as new technology or partial New Zealand ownership. This change will better ensure that farmland is preserved for future generations of New Zealanders. This higher threshold will fit within my proposed changes to the benefits test and counterfactual test. As part this reform, I am also considering refining the definition of 'farmland' to ensure its scope is clear.

Ensuring that farmland is advertised to New Zealanders

39. Recognising farmland's special status, the Act currently requires that it must be advertised for sale on the open market before consent can be given to an overseas person to acquire it. This requirement intends to ensure that New Zealanders have the opportunity to acquire, enjoy and use farmland. However, the current advertising requirements are overly complex and are not meeting the Act's objectives. The prescribed forms of advertising are outdated and therefore ineffective (for example, a placard placed at a farm gate would fulfil the existing requirements). Moreover, the advertising is not always genuine as advertising can occur after the overseas person has entered into an agreement to acquire the land. The process lacks the flexibility to allow an alternate form of advertising that may be better suited to the circumstances.

40. To complement my proposals to restrict the sale of farmland, I propose to improve these advertising requirements and the process for exemptions to ensure they meet their objectives by:

40.1. updating the prescribed forms of advertising, increasing the minimum advertising period, and specifying that the advertising must occur before any agreement (formal or informal) is entered into

40.2. clarifying that the regulator can approve alternate forms of advertising in certain circumstances to ensure that advertising is appropriate for the type of asset being sold (for example, traditional forms of advertising may not be appropriate for a sale of shares in a large company that holds some farmland)

40.3. clarifying that the type of interest in land being acquired must be the same as is being offered for acquisition on the open market (for example, if the vendor is offering a 50-year lease, then a 50-year lease, not a sale, must be advertised), and

40.4. improving the process for exemptions from the requirement, by clarifying that:

40.4.1. the Minister can impose conditions on exemptions to ensure that they are not being used to circumvent advertising requirements, and

40.4.2. an exemption application may be submitted and decided before an application for consent is lodged and that the regulator can charge a fee for doing so.

Completing the Queen's Chain

41. Public ownership of and access to our waterways is important to New Zealanders. For this reason, the Act recognises the offer of foreshore, seabed, riverbed and lakebed ('special land') to the Crown before being sold to an overseas buyer as a benefit that can be taken into account when granting consent. However, the process for offering special land to the Crown is complex, costly and time-consuming. Therefore, the Crown has not yet been able to gain ownership of any special land it has been offered. The special land provisions are also undermining the objectives of the special forestry test, introduced in October 2018, which was to streamline overseas investment in the forestry sector and support the Government in the delivery of the One Billion Trees programme.

[1]

[31]

43. I also seek Cabinet's views on whether the offer of special land to the Crown as a precondition to sale of sensitive land to overseas persons should be voluntary or mandatory.

44. Either option would resolve ambiguity in the current regime as to whether these requirements are mandatory or voluntary (except in respect of the special land provisions in the special forestry test, which are mandatory). Adopting a voluntary approach across the Act would better ensure that the special forestry test is achieving its objectives and support high-quality foreign investment more broadly. At the same time, it would likely reduce the amount of special land offered to the Crown, reducing the possibility of the Crown completing the Queen's chain.

7 And in the case of foreshore and seabed, to the common marine and coastal area in accordance with the Marine and Coastal Area (Takutai Moana) Act 2011.

45. In addition to clarifying the status of the special land provisions, I also propose to amend the Act and the Overseas Investment Regulations 2005 (the 'Regulations') to improve the process via which special land is transferred so that it works more effectively (for example, clarifying that foreshore and seabed would be transferred to the common marine and coastal area).

46. The full detail of my other proposals to reform the special land provisions are set out in Appendix 1.

47. There is an outstanding question about whether riverbed and lakebed should be administered as Crown land under the Land Act 1948 or as conservation land under the Conservation Act 1987. I will work with the Minister of Land Information and the Minister of Conservation to resolve these questions, and any other design matters that may arise during the drafting process.

Strengthening the government's ability to manage risks to security and other national interests

The regime does not effectively manage national security and other national interest risks

48. The Act does not allow the government to decline any investment in sensitive assets that is contrary to New Zealand's national interest. This risk is particularly stark in respect of investments in significant business assets, where consideration is limited to the investor's character, financial commitment, and expertise. In contrast, the Australian regime allows for a more holistic assessment across all screened transactions.

49. Further, the government cannot manage significant risks posed by investments not ordinarily screened under the Act, such as [1]

50. In particular, the Act does not:

50.1. allow decision-makers to consider potential risks to national security or public order[8] when determining whether consent should be granted

50.2. allow the government to consider whether investments in significant business assets are beneficial or not, despite investments in strategically important industries (such as transport and media) providing opportunities for espionage or sabotage

50.3. distinguish between non-government and government investors (recognising that government investors may have broader strategic, rather than commercial, foreign investment objectives)

50.4. manage any risks to national security and public order presented by investments not currently subject to screening, such as investments in small firms developing

[36]

advanced dual-use technology (that is, technology with both civilian and military applications), or

50.5. facilitate the exchange of information that could limit the use of foreign investment as a method of laundering money or financing terrorism in New Zealand.

51. This is particularly concerning given that:

[1]

[1], [33]

52. In addition, the Act does not clearly empower ministers to deny consent to transactions that could present risks of substantial economic harm or other risks to New Zealand, such as:

52.1. investments in critical infrastructure (for example, electricity and water distribution networks)

52.2. entities that link New Zealand to global value and distribution networks, or

52.3. transactions that would result in a significant portion of an industry or supply chain being owned by a limited number of entities.

Introduce a 'back stop' national interest test for assets already screened

53. To help resolve these problems, I propose to introduce a backstop national interest test, under which any investment ordinarily screened under the Act and found contrary to New Zealand's national interest (which incorporates consideration of our economic, security and other interests) could be declined. This is similar to the national interest test that underpins Australia's foreign investment screening regime.

54. To signal the test's importance and provide investors with certainty, I propose that this test would automatically apply to investments that always warrant greater scrutiny - investments where a foreign government or its associates would hold a 10% or greater interest (excluding investments involving residential land not sensitive for any other reason); investments that present national security risks; and investments in

strategically important industries and high-risk critical national infrastructure ('CNI').[9] These are detailed in Appendix 2 and would be prescribed and refined in regulations.

55. Other transactions posing significant risk to New Zealand could be subject to the national interest test on a case-by-case basis, with the agreement of the Minister responsible for exercising the national interest test (see paragraph 72). This could include, for example, investments in entities that would result in a limited number of entities owning a significant portion of an industry or a supply chain.

Complement the national interest test with a 'call in power' to manage transactions not ordinarily screened

56. The national interest test would apply only to assets already screened under the Act. It would not enable the government to manage risks posed by investments in strategically important assets that are not screened by the Act (for example, assets worth less than $100 million that do not include sensitive land). Risks can primarily emerge through an overseas person gaining access to, or control over, such an asset.

[1]

[1], [33]

[1]

57. To resolve this problem, I propose to introduce a new power (the 'call in power') to manage national security and public order risks that may be posed by such transactions. International agreements that generally restrict New Zealand's ability to screen additional classes of investment provide exceptions for measures that address certain types of national security concerns, and some agreements also allow for measures to address public order concerns.

9 CNI is the systems, assets, facilities and networks and their related supply chains that underpin the wellbeing of New Zealanders now, and into the future, because they impact on: New Zealand society and the day-to-day lives of New Zealanders, the maintenance of public safety and security, New Zealand's short and long term economic prosperity and New Zealand's international reputation.

[36]

58. The call in power would allow the relevant minister to call in certain transactions for review, and place conditions on, block or unwind (that is, require divestment of) those that present significant risks of harm to New Zealand's national security or public order. It would apply to the same categories of strategically important assets as those automatically subject to the national interest test, excluding irrigation schemes, but with the addition of entities with access to or control of sensitive data (for example, sensitive core personal data of New Zealanders). These categories would be prescribed in legislation, with additional detail provided in regulations.

59. For transactions involving certain categories of high-risk assets (such as military technology), it would be compulsory to notify the regulator of the transaction so that it can be formally reviewed. For other transactions covered by the call in power, such as those in certain CNI, notification would be voluntary. For transactions with voluntary notification, investors could choose to notify the regulator of the transaction. The government will then conduct a review, and if no problems are found, the government forgoes the right to take action in respect of that transaction in the future. If they do not notify, and problems are later found, the government can require disposal of the asset.

60. Additional detail on the proposed power's coverage, investment 'trigger levels'[11], notification mechanisms, and decision making framework are summarised in Table 1. Additional detail is contained in Appendix 3.

[1]

Table 1: Overview of proposed national security and public order call in power

Assets or entities within scope:	**Military and dual use technology**	**Critical direct suppliers to defence and security services**	**Sensitive data**	**Media**	**Critical national infrastructure**
Notification mechanism:	Compulsory	Compulsory	Voluntary	Voluntary	Voluntary
Trigger level (excluding the acquisition of listed equity securities that do not grant a disproportionate level of access or control):	0% interest	0% interest	0% interest	25% interest	0% interest
Trigger level for the acquisition of listed equity securities	10% interest	10% interest	10% interest	25% interest	10% interest

11 That is, the level of investment that must be made in an entity covered by the call in power before it becomes subject to potential review.
[36]

Decision-making framework	The decision maker must consider New Zealand's international obligations and the extent to which any risks to national security or public order can be mitigated by conditions of consent. The decision maker may also consider the economic or other benefits to New Zealand arising from the transaction.

62. A particular design feature of the call in power has required consideration against the Legislation Guidelines. I have proposed that if transactions subject to a voluntary notification regime are not notified at the point the transaction takes place, they may be called in at a later point and on rare occasions the transaction may need to be unwound. The Legislation Guidelines state that "the Government should not take a person's property without a good justification, rigorously fair procedure is required, and compensation should generally be paid…". I consider that there is good justification for unwinding transactions where they pose a material risk to New Zealand's national security and public order. I note that the Act already has provision for transactions to be unwound for breaches of the Act, and the call in power will be designed to be used in narrow circumstances, and will follow a robust and fair process that is subject to judicial review. I also note that such powers are a common feature of national security screening regimes globally to ensure that they are effective.

Options for operationalising the call in power

63. I would appreciate guidance from Cabinet on how to operationalise the call in power. There are broadly two options.

[1]

[33]

[1]

[1]

Administration of the national interest test and call in power

71. The national interest test and call in power are intended to be reserve powers, exercised rarely and only when necessary to mitigate material risks that cannot be managed through other mechanisms. [1]

72. To help manage these risks, I propose that there be a senior decision-making Minister, who does not ordinarily make decisions on transactions covered by the Act, responsible for exercising both powers. There would also be a range of transparency and review mechanisms in place to provide investors with confidence that the powers will not be used often or to manage less than significant risks to our national interests. I also propose that the regulator (the OIO) provide advice to the decision making Minister on the operation of these tests. Additional detail on these mechanisms is set out in Appendix 3.

Information exchange to ensure compliance with Anti-Money Laundering Countering Financing of Terrorism Act 2009 ('AML/CFT Act')

73. Investments in property and business can be misused for money laundering and the proposed national interest test and call in power will allow these risks to be better managed. I therefore propose that the regulator be able to exchange information collected under the Act with other regulators and the Police (in accordance with information sharing powers) as necessary to ensure compliance with the AML/CFT Act.[13]

13 In practical terms, this could be achieved by listing the Overseas Investment Act in section 140 of the AML/CFT Act.

[33]

Gaps in judicial process and enforcement

National security proposals may lead to national security information coming before the Court

75. My proposals to introduce new tests to manage national security and public order risks associated with foreign investment will introduce additional litigation risks around judicial review and disclosure of national security information to the foreign investor via the courts. I propose to maintain judicial review of decisions taken under the Act: doing so helps New Zealand compete with other jurisdictions for investment, and signals New Zealand's commitment to the rule of law. While judicial review may slow down some applications, it will improve the system overall.

76. As the national interest test and call in power are designed to mitigate risks from foreign investment, it is likely that decision-makers will rely on national security information. It is critical that this information is protected in court proceedings. [33]

I propose that the Act protect national security information, [33] and otherwise broadly aligned with those in existing legislation such as in the Telecommunications (Interception Capability and Security) Act 2013.

77. Broadly speaking, the proposed model would:

77.1. give the executive a binding decision on what information is national security information

77.2. oblige the Crown to disclose to the court any national security information that is relevant to the proceedings

77.3. oblige the court to protect that information, and

77.4. provide for a security-cleared special advocate to protect the rights of the non-Crown party.

78. This framework will protect national security information in court proceedings, preserve the right to natural justice and procedural fairness to the extent possible (given that information is being withheld from an affected person), and minimise changes for both regulators and the regulated community [33]

There are limits to the effectiveness of the regulator's current enforcement tools

79. Stronger enforcement powers will improve the government's ability to manage the risks of overseas investment. The OIO is building its enforcement function, and indicates that court proceedings and judicial decisions will remain the cornerstone of its enforcement strategy.

80. The regulator has enforcement tools that are effective for responding to relatively serious breaches that warrant disposal of the investment, and low-level breaches that require less formal tools, such as amnesty notices, to drive compliance. However the current tools do not allow the regulator to effectively respond to:

80.1. mid-level breaches, which require sufficiently serious sanctions to deter future non-compliant behaviour but do not warrant court action. The regulator's principal tool in such circumstances, settlement agreements, are of limited effectiveness in responding to such breaches because they are not directly enforceable [36]

80.2. breaches where the current maximum level of pecuniary penalty ($300,000) may not sufficiently deter non-compliance, and

80.3. specific national security and public order risks.

81. Stronger enforcement powers will improve the Crown's ability to manage the risks of overseas investment, and provide the regulator (and other actors in the system) with greater clarity as to how it can respond to a breach. To that end, I propose to provide the regulator with the following additional enforcement powers:

81.1. *Enforceable undertakings*: Statutorily empower the regulator to accept undertakings that would be directly enforceable in court, and enable it to seek certain other orders related to the enforcement of the undertaking. I also propose to establish maximum pecuniary penalties for a breach of an undertaking of $300,000 for a corporate investor and $50,000 for an individual investor. These are set at lower monetary levels than the proposed maximum pecuniary penalties available for general breaches of the Act (see paragraph 81.2). This is broadly consistent with the penalty framework under the Telecommunications Act 2001. This power would better equip the regulator to respond to mid-level breaches.

81.2. *Pecuniary penalties*: Differentiate the pecuniary penalties for individuals and corporate investors, and raise the upper threshold for each to $500,000 for individuals and to $10 million for corporate investors. This is consistent with the penalty framework under the Commerce Act 1986.

81.3. *Injunctive relief*: Specify that the regulator has an explicit ability to seek injunctive relief – that is, to clarify that it may seek urgent orders from the High Court requiring an investor to take (or not take) certain steps, with the statutory

provisions that are normal for regulators (such as the Commerce Commission and Financial Markets Authority) seeking injunctive relief.[14]

82. I consider that there may be rare occasions where the most appropriate response to national security and public order risks posed by a particular investment is to require divestment. In such circumstances, it will be necessary to act swiftly to avoid ongoing risk. Accordingly, I propose that the responsible Minister be able to seek an Order in Council for managed disposal of an investment that is creating national security or public order risks, relying on powers currently available in the Corporations (Investigation and Management) Act 1989. To give investors confidence that such a power would not be used injudiciously, the Minister's decision to seek an Order in Council would be subject to judicial review.

83. This new measure would allow for the appointment of a statutory manager, who can run a business pending its divestment and also oversee divestment. This power would be useful where the investment concerned is of significant importance for New Zealand, such as a piece of CNI.

Cutting unnecessary red tape

84. The Act screens a much broader range of transactions than other similar countries such as Australia and Canada. In many cases, screening contributes to the government's ability to manage risks associated with overseas ownership of our most sensitive assets and my proposals will improve the Act in this regard. However, in some cases the Act also imposes unnecessary red tape, by:

84.1. imposing rigorous, extensive screening that can be disproportionate to risks being managed, and

84.2. screening transactions where it is not clear what risk is being managed, or the risk is so low that screening is difficult to justify.

85. To balance my proposals to manage risks associated with overseas investment, I propose to remove this unnecessary red tape, and increase New Zealand's attractiveness to the high quality foreign investment we need, by:

85.1. simplifying the regime without compromising our ability to consider material risks, and

85.2. removing screening requirements for transactions that pose little-to-no risk.

Simplifying the regime

86. The Act's consent framework generally requires that overseas persons investing in sensitive assets satisfy the investor test, and, in respect of investments in sensitive

14 For example, the Commerce Act 1986 and the Financial Markets Authority Act 2011 specify that the Court may, on the application of the regulator, grant an injunction restraining a person from engaging in certain kinds of conduct that would constitute a contravention of the relevant legislation or from being otherwise involved in a contravention.

land[15] and fishing quota,[16] the 'benefit to New Zealand' test (the 'benefits test'). These tests aim to ensure overseas investment will be beneficial, but are the primary drivers of the Act's complexity and cost.

Ensuring the investor test focuses on material risks

87. The investor test applies to almost all transactions. It assesses an overseas person's suitability for investing in New Zealand, but applies to investors we are not concerned about (New Zealanders) and does not apply to corporate entities (unless their actions can be attributed to an individual). It also imposes unnecessary costs by enabling enquiries into matters that are not relevant to determining whether to grant consent. This has resulted in the regulator spending excessive time enquiring into low risk matters.

88. I propose a new, simplified investor test that includes a clear purpose statement, targets the right investors (including upstream corporate entities), considers only relevant matters, and does not require repeat investors to satisfy the test for each investment they make. In particular, this test would:

88.1. only consider serious, proven, offending and contraventions and enforceable undertakings (including those taken under the Act), with consideration of such conduct limited to the last 10 years unless the offence was punished by a five year or greater term of imprisonment

88.2. no longer enable open-ended enquiries into alleged behaviour, with consideration limited to allegations of offences detailed at paragraph 88.1 where formal proceedings have commenced, and

88.3. no longer be applied to New Zealanders or to investors that have previously satisfied the test's requirements (as long as their capability and/or character has not changed), but would be applied to corporate entities involved in the transaction (such as the investor and its parent company).

89. Additional detail on my proposed changes to the investor test are included at Appendix 5.

90. These changes will ensure the regime focuses on significant risks that may lead to consent being declined. This will result in timelier decision-making without significantly compromising the government's ability to manage risk. These changes will also reduce discretion to consider a wide range of actual or alleged misconduct that is unlikely to lead to an investor being denied consent. Such a broad discretion can be useful, but is difficult to operationalise sensibly and can drive enquiries into low-level risks.

Simplifying the benefits test

15 Other than some residential land, some forestry applications, and applications under the 'intention to reside' pathway.

16 Overseas persons investing in fishing quota must satisfy a 'national interest' test, which is similar to the benefits test.

91. The benefits test applies to most transactions involving sensitive land (and in a modified way, fishing quota). The test requires decision-makers to assess the benefits of a prospective investment to New Zealand by reference to up to 21 narrowly framed economic, environmental and cultural factors. This assessment is often against the counterfactual of a "competent and adequately funded alternative New Zealand purchaser" (the 'counterfactual test'). Many of the factors overlap and the counterfactual is often entirely theoretical, which makes the test unclear and unnecessarily complex. This complexity contributes towards the long timeframes for consent.

92. I propose simplifying the test by:

92.1. narrowing the number of factors it includes (without reducing its scope)

92.2. removing the ability to add factors to the benefits test by regulation

92.3. clarifying that the test is positively framed (that is, it is only used to consider benefits), subject to Cabinet's direction on an alternative option to also consider actual or likely environmental harms for certain land

92.4. better providing for Māori cultural values by recognising that protecting or enhancing wāhi tūpuna, wāhi tapu areas and Māori reservations and providing, protecting or enhancing access across land for the purposes of stewardship of historic heritage or a natural resource are potential benefits of an investment

92.5. simplifying the counterfactual to reduce the test's theoretical nature, and

92.6. requiring benefits offered to be proportionate to the sensitivity of the interest in land being acquired.

93. The test proposed above would include a factor that can be used to assess an investment's benefits to the physical and natural resources on the relevant land, or on other land as a result of activities occurring on the relevant land (for example, pest control or weed management).[17] This would enhance the government's ability to manage environmental concerns, including concerns related to water quality and use, relative to the status quo. Consistent with paragraph 92.3, it would not allow any likely or actual environmental harms resulting from an investment to be explicitly considered when determining whether to consent to an investment.

94. An alternative option would be to enable Ministers to consider, in addition to likely or actual environmental benefits, likely or actual environmental harms when assessing applications to acquire non-urban land of greater than five hectares (given the high value). I seek Cabinet's guidance on this matter.

95. Incorporating such a factor into the benefits test would explicitly allow Ministers to weigh any environmental harms associated with such an investment (such as a reduction in water quality) against environmental and other benefits before determining whether an investment is of benefit to New Zealand. Before the existence

17 In respect of investments in fishing quota, the environmental factor would relate to that type of investment.

of such likely or actual harms could be weighed as part of the benefits test, consideration would need to be given to whether conditions could be imposed on the prospective investment to mitigate, or remediate, any likely or actual environmental harms.

96. Including such a factor in the benefits test has a number of risks. It could reduce the Act's coherence, increase complexity and costs for the regulator and applicants, and increase the chance of inconsistent decision making across different regulatory regimes in respect of similar activities (such as the Resource Management Act 1991 ('RMA')). However, I recognise that it may enhance the government's ability to manage environmental risks associated with foreign investment and provide the Government with a means to respond to the high level of public interest and concern about this matter reflected during public consultation. It would also provide an opportunity to manage concerns relating to water.

97. A more targeted option to allow consideration of environmental harms in certain circumstances (that would not pose the same risks as the broader approach described above), would be to allow consideration of an investment's positive or negative effects on water quality and sustainability, where the investment involves water bottling, or bulk water export for human consumption on sensitive land. This option would enhance the government's ability to manage environmental risks associated with foreign investment and respond to the environmental issue that much of the concern during public consultation centred on – water bottling. As a smaller number of transactions would be affected, this would have less of an impact on the Act's coherence, complexity and costs for the regulator and applicant, and have a reduced risk of inconsistent decision making across different regulatory regimes than the previous alternative option. For this reason, I recommend adopting this option over a more comprehensive environmental harm factor.

98. This would not completely address public concerns around water bottling, because it would only apply to transactions on sensitive land. Despite this, if Cabinet were to allow greater consideration of environmental harms under the Act, I consider that this is the best way to achieve this without risking the reform's broader objectives.

99. I further note that while, during consultation, some submitters suggested that water be made a new class of sensitive asset subject to screening under the Act, this would raise issues of consistency with New Zealand's international obligations.

100. Any of these alternative options, if adopted, would be complementary to other remedies the Government is considering, including a royalty on water, [33]

101. The proposed simplifications will not reduce the government's ability to manage risk and, as noted earlier, farmland will be subject to higher thresholds within this test. Additional detail on these proposals is included in Appendix 6.

Impose timeframes on decision-making

102. New Zealand's screening regime differs from those in almost all other comparable countries by not requiring decisions on applications within a specified timeframe.

103. Unsurprisingly, this has enabled an iterative process to improve lower-quality applications so that they meet the Act's requirements, and does not incentivise decision-makers to provide investors with certainty about their application. This, combined with complex tests, has led to long timeframes for decision-making, which, more than any other element of the regime, discourages investment in New Zealand.

104. I propose to introduce tailored timeframes for different types of decisions (which will be prescribed in regulations, following consultation with agencies) to bring us into line with other regimes. These changes will require decision-makers to arrive at decisions more quickly than they are currently, and decision-makers will be required to publicly report on their compliance with statutory timeframes. However, decisions will not be void if they are made outside those timeframes, and the Crown will not be liable for any loss suffered by applicants as a result of breaching a timeframe. Risks from introducing timeframes should be mitigated by:

104.1. the regulator having a preliminary period to review transactions before accepting an application and statutory timeframes commencing (and being able to charge a fee for this), and being empowered to not accept those that do not provide adequate information

104.2. other changes I am proposing as part of the reform, which will streamline the consent process (noting the option of considering environmental harms, might, if adopted by Cabinet, offset some of these gains)

104.3. in certain circumstances, an ability to extend timeframes (either by a prescribed or agreed period). For example, extensions could be used to deal with complex applications and where necessary to deal with workload pressures during peak periods, and

104.4. incentivising investors to raise the standard of their initial applications by reducing the regulator's scope to go through an iterative process with low quality applications. If applications do not meet the required standard, the regulator will propose that they be declined.

Removing screening requirements for less-sensitive transactions

105. There are cases where screening is unnecessary and the compliance costs are disproportionate to the (minimal) risks being managed. This can be because the Act:

105.1. covers some assets or interests in assets that are not particularly sensitive, such as short to medium term leases

105.2. screens some entities which are, by most other measures, fundamentally New Zealand entities, such as companies that are majority-owned by New Zealanders, and

105.3. screens small changes in shareholding that do not materially impact on the ownership or control of the sensitive assets, such as requiring screening for small investments that result in a company becoming an overseas person.

106. I propose to reduce this overreach by no longer screening a range of lower risk transactions. Reducing the number of transactions that are screened will encourage productive investment in New Zealand, while ensuring that the Act and the regulator focus on transactions that pose a material risk to New Zealand.

Removing short-to-medium term leases from the regime

107. Leases and other 'less-than-freehold' interests (for example, a mortgage) in sensitive land are subject to screening if their term is three years or more, including any rights of renewal. This reflects that leases have many of the characteristics of ownership (for example, possession and, in some cases, rights to make alterations to the land). However, leases are generally less sensitive than freehold interests because the benefit of the land will return to the owner at the end of their duration. Screening shorter-term leases imposes disproportionate costs on investors relative to the risks being managed and, perversely, can create incentives for overseas persons to purchase land outright (because the process and cost to get consent are the same).

108. I propose to increase the threshold for when leases are screened to 10 years or more (including any right of renewal, and situations where this threshold is reached in a single lease or consecutive leases) for sensitive land other than residential land. This change would be most beneficial for commercial leases and some industrial leases, which frequently last for three years with two rights of renewal (nine years in total). While, in rare cases, there may be some reduction in the government's ability to manage risk, it would still capture most rural leases (for instance, land for agriculture, horticulture or viticulture), which are generally for longer terms.

109. There is an additional problem with the Act's treatment of periodic leases (that is, leases that do not have a set end date). Periodic leases were never screened, and were never intended to be screened, under the Act. Phase One clarified that periodic leases over residential land were not to be screened but did not address other types of sensitive land, which has resulted in uncertainty as to their treatment. To resolve this, I propose clarifying that periodic leases are not an interest in land that requires screening.

Removing low-risk sensitive adjoining land from the regime

110. The Act requires transactions to be screened if they involve land that adjoins other land that has sensitive characteristics ('sensitive adjoining land'), such as the foreshore, a lakebed, some types of conservation land, historic places and wāhi tapu (sacred places). Screening seeks to ensure that transactions are beneficial to the conservation of, or public access to, the sensitive adjoining land. Problems with the regime are described below.

110.1. Sensitive adjoining land is screened even when there is no prospect of achieving meaningful access or environmental benefits, because there are no

environmental concerns or access problems with the sensitive land it adjoins (for example, a park or reserve, which can be easily accessed). Screening in these cases takes time and money, and discourages investment without addressing any risk.

110.2. Screening requirements can be arbitrary and inconsistent because it can depend on how land is designated by the relevant local authority. For example, I am aware of land being purchased for a supermarket that required screening because it adjoined a grass berm classified as a reserve.

110.3. The risks associated with the purchase of sensitive adjoining land are not specific to overseas investment. The RMA regulates land use, including impacts on adjoining land.

111. I propose to limit sensitive adjoining land to land adjoining the foreshore, lakebed, conservation land and regional parks[18], and some land significant to Māori[19]. This would streamline the current regime by removing categories of land with no obvious sensitivies from screening requirements. While this may limit the regulator's ability to negotiate access conditions in rare cases, in practice these conditions are rarely applied and, in the vast majority of the cases, they involve land that is sensitive in its own right. The regulator would still retain the ability to screen land that adjoins truly sensitive land where significant benefits can be gained in terms of access or environmental or cultural protections.

Ensuring some fundamentally New Zealand entities are not overseas persons

112. The way the Act currently defines overseas persons works well for individuals but not always as well for legal persons like companies, and managed investment schemes. A company is an overseas person if it is 25% or more owned or controlled by one or more overseas persons. Equally, a managed investment scheme will be an overseas person if it is managed by an overseas person (even if it is investing on behalf of New Zealanders who could buy sensitive assets in their own right without obtaining consent).

113. These definitions lead to some entities and managed investment schemes that most New Zealanders would consider to be fundamentally New Zealand entities, and that are majority owned/funded by New Zealanders, being overseas persons (for example, default KiwiSaver providers managed by subsidiaries of Australian banks, and, in the case of listed companies, Air New Zealand and Ryman Healthcare). Requiring these entities to obtain consent is inconsistent with the Act's purpose and stifles the growth of New Zealand's capital markets, which rely on foreign capital.

18 Including land held for conservation purposes under the Conservation Act 1987 (if that conservation land exceeds 0.4 hectares in area), any reserve under the Reserves Act 1977 that is administered by the Department of Conservation and that exceeds 0.4 hectares in area, regional parks that exceed 80 hectares in area, and national parks.

19 Including (all exceeding 0.4 hectares in area) Māori reservations that adjoin the sea or a lake and to which section 340 of Te Ture Whenua Māori Act 1993 applies; land that is set apart as a Māori reservation and that is wāhi tapu under section 338 of Te Ture Whenua Māori Act 1993; wāhi tapu or a wāhi tapu area that is entered on the New Zealand Heritage List/Rārangi Kōrero or for which there is an application that is notified under section 67(4) or 68(4) of the Heritage New Zealand Pouhere Taonga Act 2014; any reserve under the Reserves Act 1977 managed wholly or jointly by the governance entity of a collective group of Māori such as an iwi or hapu; public conservation land that has been used as cultural redress in a Treaty settlement and has retained conservation protection.

114. I propose removing some fundamentally New Zealand entities from the definition of overseas person so they are not subject to screening requirements. My proposals include:

114.1. treating listed companies that are majority owned by New Zealanders, and which overseas persons are unlikely to be able to exert negative control[20] over, as New Zealand entities, and

114.2. introducing exemptions from screening requirements that non-listed entities and managed investment schemes may apply for if they are similarly majority owned by New Zealanders, overseas persons are unlikely to be able to exert negative control, have a strong record of compliance and are not subject to material influence by any foreign government.[21]

115. These proposals and some other minor changes to improve the Act's coherence are set out in more detail in Appendix 7.

Ensuring low risk transactions are not subject to screening

116. I also propose to make changes to limit the number of small transactions, which pose little risk, that are screened. This will increase New Zealand's attractiveness to foreign investment, particularly in New Zealand's capital markets where smaller transactions are more common and screening can serve as a barrier to investment (as the costs greatly outweigh potential gains on many transactions). My proposals include removing screening requirements for:

116.1. some transactions entered into by overseas persons with a non-material interest in a listed company where the transaction results in that entity becoming an overseas person

116.2. some smaller transactions that do not materially change an overseas person's level of control, and

116.3. transactions involving interests that do not grant any control over the sensitive asset, such as transactions that support the issuance of financial products that support New Zealand's financial stability.

117. Each of my proposals are set out in more detail in Appendix 8.

Exemption making power

118. My proposals to introduce new exemptions will require amendment to the exemption criteria in the Act to enable relevant changes to the Regulations.

20 An interest in more than 25% of an entity's security (that grant control rights) gives an overseas person negative control. A person with negative control can prevent a company from passing special resolutions which is required to amend a company's constitution and enter into 'major transactions'.

21 That is, a foreign government does not have a 10% or greater interest in the entity/fund or a lesser interest that grants a disproportionate level of control over, or access to, the relevant investor.

Acquisition of fishing quota

119. The Fisheries Act 1996 (the 'Fisheries Act') requires overseas investors to obtain consent to acquire an interest in fishing quota.[22]

120. The consent requirements are similar to those in place for the purchase of sensitive land (that is, investors must satisfy the investor test and a test similar to the 'benefit to New Zealand' test, the 'national interest test'). The legislative provisions setting out these consent requirements are split between the Fisheries Act and the Act.

121. To ensure that the process to obtain consent to fishing quota remains consistent with the process for purchasing sensitive land (excluding farmland), I propose that:

121.1. any changes to the investor test (paragraph 88) be reflected in equivalent provisions of the Fisheries Act

121.2. the factors in the Fisheries Act's 'national interest test' be aligned with the broad factors I am proposing to be included in the benefit to New Zealand test (see paragraph 92)

121.3. the Fisheries Act's 'national interest test' be renamed the 'benefit to New Zealand test', to harmonise it with that test in the Act, and

121.4. the Fisheries Act make clear that, if adopted, the proposed 'back stop' national interest test (see paragraph 53) can be applied to prospective investments in fishing quota.

Operationalising the reforms

122. These reforms will recalibrate the level of screening away from a regime requiring comprehensive enquiry into a broad range of risks, to one where the depth of enquiry will be more proportionate to the risk posed. This will enable the regulator to focus its enquiry on material risks only. This is balanced with providing additional tools to respond to investments posing significant risks to the national interest and to manage national security and public order risks not presently covered by the overseas investment regime.

123. Significant operational changes will be needed to ensure these reforms are successful. In particular:

123.1. Applicants will need to deliver high-quality applications, to support faster decision-making: if applications are incomplete or do not show sufficient benefit, they will likely be declined.

123.2. The context for decision-making will need to shift from one where there is an obligation to consider all possible risks that an investor might pose, to one that requires consideration of material risks only, and making those assessments more quickly.

22 The Fisheries Act defines an "interest in fishing quota" to include provisional catch history, quota, or annual catch entitlement, or an interest in the same

123.3. The national interest test and call in power are intended to be reserve powers. It will be critical to ensure that initial risk assessment is calibrated appropriately and consistently with whichever operational model is adopted so that only the highest-risk applications are subject to this additional scrutiny.

123.4. The regulator will need new funding to build capability, including new systems and business process to operationalise the reforms as a whole, including its new functions and powers (as set out in the financial implications section of this paper).

124. The regulated parties will require a high level of certainty about when the new national interest test and call in power will be applied and what degree of information will be needed by the regulator and decision-makers. Careful legislative and regulatory drafting will provide the necessary certainty for the regulator, decision-makers and investors on the categories of assets and types of transactions that will be subject to these new reserve powers. In addition new guidance and communication with the investment community about these new aspects of the regime will be required.

125. To ensure these operational changes and guidance are in place, there will be an implementation period prior to the Act coming into force. This is likely to be 12 months (though there is potential for more straight-forward changes to come into force earlier). The exact timing will be confirmed on introduction.

Additional policy decisions

126. Due to the complexity of these policy matters and interaction with other legislation and government priorities, I expect that additional policy decisions will have to be made during the drafting of amendments to the relevant legislation. The Terms of Reference also specified that the Phase Two reform's scope includes addressing any minor technical amendments required to resolve unintended consequences associated with the implementation of Phase One. I also expect to make decisions on these minor and technical points during drafting.

127. In addition, this Cabinet paper does not address:

127.1. how tax is considered as part of screening (other than that tax offences will be considered as part of the investor test). The Terms of Reference asked for consideration of whether to include tax considerations in the screening process, and options were included in the consultation document. I have sought further advice from Treasury and Inland Revenue on this issue

127.2. proposals to support information sharing between the regulator and other relevant agencies, and

127.3. in relation to special land: which legislation, and agency, should administer riverbed and lakebed.

128. I propose that Cabinet authorise me to:

128.1. take additional policy decisions that may arise during the drafting of the legislation. This may include minor technical changes relating to the implementation of Phase One

128.2. take any policy decisions on whether and to what extent tax should be considered part of the screening process, in consultation with the Minister of Revenue, the Minister of Finance, Associate Minister of Finance (Hon Dr Clark), Minister of Land Information, and Associate Minister of Finance (Hon Jones)

128.3. take policy decisions on proposals to support information sharing between the regulator and other agencies [33]
in consultation with the Ministers from affected departments, and

128.4. take policy decisions on which legislation, and agency, should administer riverbed and lakebed; and any other design matters which may arise in relation to the special land provisions during the drafting process, in consultation with the Minister of Land Information and the Minister of Conservation.

Review of the Phase Two reform

129. It is my intention that the Treasury begin a review of the new call in power three years after its commencement, and the balance of these reforms five years after their commencement. This staggered review timeframe will provide an early opportunity to review the most significant addition to the Act. For the remaining reforms, it will allow the new regime to bed in, and enable time for data collection, monitoring and evaluation. It will also give certainty to the regulated community that significant changes will not be made in the early days of the new regime's operation.

International implications

[36]

[36]

Call in power

[36]

[1]

133. The property rights of an owner of New Zealand land do not extend to the right to sell land to an overseas person. [36]

[36]

Departmental consultation

138. The following departments have been consulted on this paper: Department of the Prime Minister and Cabinet (National Security Group and Policy Advisory Group), Government Communications Security Bureau ('GCSB'), New Zealand Security Intelligence Service ('NZSIS'), MFAT, Land Information New Zealand (including the OIO), 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, New Zealand Defence Force, New Zealand Police and the Crown Law Office.

[1]

Financial Implications

[1], [33]

[33]

[1], [33]

[33]

145. In considering the financial implications of the reform, there is a need to be conscious of the overall financial situation of the OIO. The OIO is currently operating a significant deficit per year and its current fee model is not fully recovering costs. The OIO memorandum account has a deficit of over $8 million and this is forecast to continue to increase by an estimated $2 million per year at current application volumes.

[33]

25 Time-limited funding to partially recover the costs of enforcement and litigation was provided as part of Phase One on the basis that some of this activity was a public good.
Treasury:4155078v17

146. As part of the funding decision for Phase One, Land Information New Zealand committed to undertake a comprehensive review of the OIO fees model within two years. Given the current financial position of the OIO and that the anticipated volumes for some of the new Phase One pathways are significantly below what was estimated, LINZ considers it prudent to undertake a fees review urgently so that new fees for the current regime can be in place for the 2020/21 financial year.

[33]

[1], [33]

[1]

[1], [33]

Legislative Implications

154. My proposals will require changes to the Act, the Regulations, the Fisheries Act, the Corporations (Investigation and Management) Act 1989, Conservation Act 1987 and the AML/CFT Act. [33]

Impact Analysis

155. The regulatory impact analysis requirements apply to the proposals in this paper and a Regulatory Impact Assessment ('RIA') has been prepared and is attached.

156. The Treasury quality assurance panel has reviewed the RIA prepared by Treasury and associated supporting material, and considers that the information and analysis summarised in the regulatory impact assessment partially meets the quality assurance criteria.

157. The quality assurance panel has commented that:

157.1. The RIA clearly describes the policy problems, objectives, options and the policy process to date. It also clearly identifies where officials' recommendations differ from the options being recommended to Cabinet, and the differing judgements and weightings behind those differing recommendations.

157.2. The RIA is clearly written but lengthy, reflecting the complexity and breadth of the issues this policy package addresses.

157.3. The review panel assessed the great majority of the RIA as meeting the quality assurance criteria. The key reason for the panel's overall assessment being the RIA partially meets the quality assurance criteria is that the proposals regarding moving the rural land directive to primary legislation do not meet the consultation requirements. These proposals have not been consulted on publicly, or with key non-Crown stakeholders, including Māori. [1]

157.4. Addressing this would require appropriate consultations, and inclusion of the results of that consultation, in the proposals being made to Cabinet.

Human Rights

158. There will be human rights implications arising from this paper.

Freedom from discrimination

159. The Act, and therefore reform 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 (the 'NZBORA').

160. I consider that this limit on the freedom of discrimination is justifiable. The Act's objective is to ensure investments by overseas persons in sensitive assets have genuine benefits for the country (recognising that it is a privilege to own or control those assets). This objective is sufficiently important to justify a limitation on the right to be free from discrimination.

161. My proposals extend the regime to capture national security and public order risks, place additional restrictions on purchases of farmland, and augment the enforcement measures available to the regulator to support better compliance with the Act's objectives. These enhancements are sufficiently important to justify any further limitation on the rights to be free of discrimination. The proposed changes are aimed at ensuring an investment genuinely benefits New Zealand, and that non-compliance may be effectively addressed. They also ensure that the government can prevent an investment where the risks ultimately outweigh those benefits, and manage any harm resulting from an investment.

162. The changes do not limit the right more than reasonably necessary. In particular:

162.1. nationality does not always determine whether a person will be an overseas person and therefore subject to screening under the Act. For example, individuals who ordinarily reside in New Zealand, regardless of their nationality, are not overseas persons

162.2. the call in power will only be exercised where there are significant risks to national security and public order

162.3. additional enforcement measures are consistent with the purposes of the Act and the proposed reforms, to assist with compliance, and

162.4. some of my proposals reduce the burden of screening or eliminate it altogether where the current level of screening is disproportionate to the level of risks posed.

Enforceable undertaking proposals engage the right to be presumed innocent until proven guilty

163. The proposal to empower the regulator to accept enforceable undertakings, without a prohibition on the undertaking constituting an admission of guilt, may engage the right to be presumed innocent until proven guilty as protected under the NZBORA.

164. However, the proposal has been formulated taking account of the ability of an investor to participate in a fair negotiation process and negotiate a condition that protects them from the enforceable undertaking being used as an admission of guilt to also bring about a prosecution (for example, by negotiating a condition of immunity from further suit). We therefore consider the potential limit on the right to the presumption of innocence is justified.

National security information before the court proposals engage the right to justice

165. NZBORA provides that every person whose interests are affected by a decision by a public authority has the right to natural justice. This right will be engaged by the proposals to amend the Act to include protections for national security information in court proceedings that are in line with existing legislation [33]

These will include allowing the court to receive or hear national security information in the absence of the non-Crown party in certain circumstances.

166. Consistent with other regimes, natural justice will be preserved to the extent possible through safeguards, including the use of security-cleared special advocates to represent the non-Crown party's interests, and by allowing the court to approve a non-classified summary of the national security information to be given to the non-Crown party. Given these safeguards, and the need to protect national security information, I consider the limitation on the right to justice is justifiable.

Special land options engage the right to hold land and right to justice

[1]

Right to hold land

168. The right to hold land in New Zealand is protected by common law and also reflected in the Universal Declaration of Human Rights. The government should only acquire land compulsorily in limited circumstances, where there is a strong policy justification and natural justice is carefully followed. Compensation should normally be available, and a cogent policy justification is required to depart from this. [1]

169. In any case, I consider that this limit on the right to hold land would have been justifiable. [1]

The RMA requires an esplanade reserve to be set aside as a pre-condition to resource consent for any subdivision. This also occurs without monetary

compensation, instead the land-owner is compensated by obtaining the right to subdivide the land. [1]

Similar provisions also already apply to foreshore and seabed.

Right to justice

170. The right to justice under the NZBORA includes the right to review any decision. [1]

Te Tiriti o Waitangi / Treaty of Waitangi ('Te Tiriti')

171. It is my view that Te Tiriti conferred upon the Crown the right to control the sale of land to overseas persons. Overseas investment rules that differ on the basis of ethnicity are likely to be divisive. I do recognise, however, that the Crown has an obligation to ensure that overseas investment does not infringe Article Two rights over taonga.

172. A significant proportion of Te Ōhanga Māori comprises assets in land-based industries such as forestry, farming (horticulture and agriculture), as well as fisheries (Te Ōhanga Māori, Te Puni Kōkiri), which can be captured as 'sensitive assets' under the Act. Māori also have strong cultural interests and values in natural resources, particularly in land and water. Agencies consider that the current law, and therefore amendments to it, is likely to disproportionately affect iwi, hapū and whānau if they wish to sell those assets to overseas persons.

173. To realise their ōhanga aspirations, iwi/Māori businesses may look to enhance the productivity of their land-based assets. Access to foreign capital can enable Māori to realise that productivity and enhance their economic prosperity, but beyond this it can bring other advantages such as the ability to integrate into global value chains and establish international relationships. This reform package includes proposals that will support these aspirations by:

173.1. reducing the compliance burden on iwi/Māori business, which look to access foreign capital to develop their asset base, and

173.2. to strengthen consideration of Māori cultural values, in relation to wāhi tūpuna and Māori reservations and access to sensitive sites, when land is screened under the Act.

174. The Treasury engaged with Māori as part of the consultation on the policy options in the consultation document. This included working with iwi/Māori representatives, practitioners and specialist advisors to invite key iwi/Māori organisations with interests likely to be affected by the reform to participate in hui across a range of locations. Feedback was sought from participants on the draft proposals, which then informed the design of the final reform package, noting some feedback, particularly from iwi

representatives, sought stronger recognition of Māori values than is reflected in the package.

175. The consultation document did not cover options to enshrine the rural land directive [1], [34]

[36]

179. However, I consider that the sovereignty conferred on the Crown under Article One of Te Tiriti grants the Crown the right to make final decisions on whether to approve the sale of sensitive land, regulated by the Act, to overseas investors (provided that such decisions are made in a manner consistent with the Crown's obligations to balance this with other considerations such as active protection of Māori rights and interest and participation by Māori in matters of concern to Māori). [36]

180. My considered view is that on balance, the overall reform package aligns with our obligations under the three Articles of Te Tiriti, to work with Māori and protect Māori interests.

Gender Implications

181. There are no gender implications arising from these proposals.

Disability Perspective

182. There are no disability implications arising from these proposals.

26 As defined in Te Ture Whenua Māori Act 1993.

27 As defined in Te Ture Whenua Māori Act 1993.

Publicity

183. I plan to publicly announce the policy decisions in this paper after they have been agreed by Cabinet.

184. The Phase Two reform aims to strike a balance between ensuring the regime effectively manages risk, and cutting red tape for low risk investment. The reform is likely to attract comment from a range of stakeholders with divergent perspectives on where we have shifted that balance. In particular, I expect that:

184.1. farmers, Māori (Māori land is largely rural) and the business community may be opposed to legislating a higher bar for investments in farmland (which was not consulted on)

184.2. the business community may also object to the broad scope and highly discretionary nature of the call in power

184.3. some individual and civil society groups that favour measures to further restrict some forms of investment are likely to oppose reducing screening requirements for some bodies corporate, and

184.4. many of New Zealand's international partners will be closely monitoring the consistency of the reforms with New Zealand's international obligations [1]

185. More generally, there may be a perception that by enshrining the rural land directive and allowing consideration of likely and actual environmental harms for certain land, the Government is tightening the rules around foreign investment in New Zealand and that New Zealand is less open to foreign investment.

186. It will therefore be important for the Government to continue to publicly articulate:

186.1. the value of foreign investment, particularly in low risk areas where changes are being proposed, and that New Zealand remains open to productive, high quality overseas investment

186.2. the need for an effective screening regime to ensure that investments in our most sensitive assets (such as our farmland) are of benefit to New Zealand, and that risks associated with investment can be effectively managed, and

186.3. the importance of screening for national security and public order, and that doing so it is consistent with our international obligations.

187. This messaging will be critical to ensuring that any amendments required to be made to the Act can proceed with broad public understanding and support. Officials have developed an engagement plan for the public announcement of these reforms,

including in particular working with MFAT to manage communications with New Zealand's international partners, before public announcements are made.

Proactive Release

188. I intend to publish this Cabinet paper 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.

189. In particular, I note my intention to redact content that is:

189.1. related to the national interest test and national security call in power. This is due to the risk that releasing this information would prejudice the security or defence of New Zealand or the international relations of the government of New Zealand, or

189.2. legally privileged.

Recommendations

I recommend the Committee:

1. **Note** on 8 October 2018, Cabinet agreed to the Terms of Reference for Phase Two of the reform of the Overseas Investment Act 2005 (the Act) [CAB-18-MIN-0481].

2. **Note** public consultation on options for the Phase Two reform of the Act ('Phase Two reform') highlighted the need for this review to:

2.1. ensure the regime more effectively manages risks posed by overseas investment, and

2.2. simplify the decision-making process and remove transactions from the regime where screening does little to improve the management of risks associated with the investment.

Ensuring the Act more effectively manages risks posed by overseas investment

More enduring protection for our farmland

3. **Note** that the special privilege involved in owning or controlling farmland is not adequately reflected in the Act.

4. **Agree** that overseas investments in farm land must generally demonstrate a substantial point of difference in their likely level of economic benefit or oversight or participation by New Zealanders to receive consent, with some exceptions, such as where transactions are minor or technical.

5. **Note** that I am considering options to more precisely define farmland.

Ensuring New Zealanders have the opportunity to acquire farmland

6. **Note** that the Act and the Overseas Investment Regulations 2005 (the 'Regulations') require vendors to advertise farm land before an overseas person can obtain an interest in it, but the current advertising requirements are outdated and not achieving the intended objectives.

7. **Agree** to strengthen the farmland advertising requirements to reduce complexity and ensure that New Zealanders have the opportunity to acquire, enjoy and use farmland, including by:

7.1. updating the list of appropriate forms of advertising, increasing the minimum advertising period, and allowing the regulator to approve alternative forms

7.2. requiring advertising to occur before a vendor enters into a transaction

7.3. clarifying that only the interest in the farmland being acquired has to be advertised

7.4. allowing the Minister to place conditions on applications for exemptions from the advertising requirements, and

7.5. enabling an application for exemption from the advertising requirements to be submitted and decided before an application for consent is lodged, and enabling the regulator to impose a fee for deciding such an application.

Completing the Queen's chain

8. **Note** the Act and the Regulations recognise the importance New Zealanders place on public ownership of or access to the foreshore, seabed, riverbed and lakebed ('special land') by providing for this land to be offered to the Crown before being sold to an overseas person.

9. **Note**, however, that the process for offering special land to the Crown is complex, costly and time-consuming, and for this reason, the Crown has not yet been able to gain ownership of any special land it has been offered.

[1]

11. In order to clarify whether the special land provisions are mandatory or voluntary, either**:**

11.1. **Agree** that offering special land to the Crown (subject to recommendation 12.6) be mandatory for all sensitive land (and remain mandatory for the special forestry test).

OR

11.2. **Agree** that offering special land to the Crown (subject to recommendation 12.6) be voluntary for all sensitive land (including land acquired under the special forestry test).

12. **Agree** to amend the process by which the Crown acquires special land so that it works more effectively, including by:

12.1. requiring the Crown to decide within a specified timeframe whether it waives the right to acquire special land

12.2. specifying the circumstances when the Crown may waive the right to acquire special land

12.3. enabling, if the Crown wishes to acquire the special land, the Crown to place a memorial on the title (at which point the special land provisions are satisfied, with a duty on the Crown to take ownership within 10 years or the memorial will lapse)

12.4. enabling standardised terms and conditions for the transfer of such special land to be prescribed in the Regulations, which would be mandatory unless the parties agree otherwise

12.5. specifying that if the Crown does not make a decision on the offer of special land within the current 30 working day timeframe, the offer is deemed to be waived, subject to a duty for the Minister to use his/her best endeavours to make a decision before then

12.6. clarifying that foreshore and seabed offered to the Crown is transferred to the common marine and coastal area in accordance with the Marine and Coastal Area Act 2011, and

12.7. confirming that the provisions apply only to the acquisition of freehold interests and perpetually renewable leasehold interests under the Crown Pastoral Land Act 1998.

13. **Note** that the Surveyor-General has indicated they are prepared to develop survey standards that adequately define the extent of the private and Crown land, to support the issue of titles with less cost and complexity.

14. **Note** that the Associate Minister of Finance (Hon Parker) will work with the Minister of Land Information and the Minister of Conservation to determine (recommendation 91.2, refers):

14.1. whether riverbed and lakebed are administered as Crown land under the Land Act 1948 or as conservation land under the Conservation Act 1987, and

14.2. any other design matter relating to special land that may arise during the drafting process.

Introduction of a national interest test

15. **Note** the Act does not allow proposed overseas investments to be declined if they are contrary to New Zealand's national interest.

16. **Agree** to introduce a 'national interest test' that would empower the relevant decision making Minister (refer recommendation 38) to decline any investment in significant business assets, sensitive land, or fishing quota (or combination thereof) found contrary to New Zealand's national interest.

17. **Agree** that the national interest test would always apply to transactions with certain high-risk characteristics, including those:

    17.1. where a foreign government or its associates would hold a 10% or greater interest (excluding transactions only including residential, but not otherwise sensitive, land)

    17.2. where the Government Communications Security Bureau or the New Zealand Secret Intelligence Service identifies them as posing a risk to national security or public order, or

    17.3. in certain strategically important industries and high-risk critical national infrastructure, as prescribed by the Minister in regulations.

18. **Agree** that the national interest test could be applied to any other transaction screened under the Act on agreement between the Act's relevant ordinary decision making minister/s and the Minister responsible for administering the national interest test (recommendation 38 refers).

Introduction of a call in power

19. **Note** that international agreements that generally restrict New Zealand's ability to screen additional classes of investment provide exceptions for certain types of national security measures, and some also allow for measures to uphold public order.

20. **Agree** to introduce a 'call in power' that would empower the government to review transactions (either prospective or concluded) in a limited set of assets (recommendation 27 refers) not ordinarily screened under the Act (a consequential change to the purpose of the Act will likely also be required).

21. **Note** that the call in power is a reserve 'back stop' power, anticipated to be rarely used, and only to manage significant risks to New Zealand's national security or public order.

[36]

24. **Agree** that the Minister can, where necessary to mitigate significant risks to New Zealand's national security or public order, impose conditions on, decline, and unwind transactions within scope of the call in power.

25. **Agree** that transactions within the scope of the call in power can only be declined or unwound if the relevant Minister has reasonable grounds to believe that it will present significant risks of harm to national security or public order, but in considering whether to decline or unwind the Minister(s):

25.1. must also have regard to:

25.1.1. New Zealand's international obligations, and

25.1.2. the extent to which any risks can be mitigated by conditions of consent, and

25.2. may have regard to economic or other benefits to New Zealand arising from the transaction.

Assets in scope of the call in power

26. **Agree** that assets covered by the call in power will be defined in legislation, with further specification in regulations to balance the need to:

26.1. provide certainty to investors

26.2. allow the government to respond to emerging risks, and

26.3. ensure that the power does not capture more transactions than necessary to manage relevant risks.

27. **Agree** that transactions in the same high risk critical national infrastructure and strategically important industries as proposed to be automatically subject to the national interest test (refer recommendation 17.3), as well as transactions involving entities with control of, or access to, sensitive data, be subject to the call in power.

28. **Agree** that before making regulations to refine the definitions of assets/entities in scope of the call in power or other legislative instruments to specify entities covered by the call in power as referred to in recommendations 27, the Minister must be satisfied that the proposed regulation is no broader than necessary to manage risks to national security or public order and is consistent with New Zealand's international obligations.

Types of transactions in scope of the call in power

29. **Note** that the 'thresholds for investment' determine what percentage of an asset must be acquired by an overseas person before the asset can be called in.

30. **Agree** that the following thresholds for investment in an asset covered by the call in power must be met before a transaction can be potentially reviewed under the call in power:

30.1. for media entities: more than 25% ownership or control of the entity's governing body or voting power

30.2. for non-publicly listed interests in all other assets covered by the call in power: 0%, and

30.3. for listed equity securities in all assets covered by the call in power, excluding media entities: transactions that result in the acquirer holding 10% or more of that class of that entity's publicly listed equity securities, unless the investment grants special access to, or control of, that target entity.

Notification requirements for the call in power

31. **Agree** that investors would be required to notify the government of transactions in scope of the call in power related to assets captured by the definition of dual-use and military technology and listed as critical direct suppliers to the New Zealand Defence Force or security services.

32. **Agree** that investors have the option of, but are not required to, notify the government of transactions in all other assets within scope of the call in power not referred to in recommendation 31, but that if they do notify the government and the government does not take any action, the government generally cannot take any action in respect of that transaction in the future.

Options to operationalise the call in power

33. To operationalise the call in power, either:

33.1. **Agree** that:

[1]

OR

33.2. **Agree** that the regulator establish an active screening regime, where the regulator [1] to identify and investigate those presenting substantial risks to national security or public order.

34. **Agree** that the responsible Minister can specify to the Chief Executive of the regulator the extent of screening (and associated costs and risks) they seek under the call in power.

[1], [33]

[1]

Administration of the national interest test and call in power

38. **Agree** that the Minister responsible for decision-making under the national interest test and the call in power would:

38.1. not be a Minister ordinarily responsible for decision-making under the Act and the Regulations, and

38.2. be unable to delegate this decision-making power to the regulator.

39. **Agree** that the Minister responsible for decision-making under the national interest test and the call in power be required to publicly report on decisions made under both tests, with exceptions such as decisions (or parts of decisions) that must remain confidential to protect national security, New Zealand's international relations, or commercial-in-confidence information.

40. **Agree** that the Minister be empowered to publish policy guidance on the types of matters likely to be considered when determining whether a transaction is contrary to New Zealand's national interest, or security and public order interests, as relevant.

41. **Agree** that the regulator be responsible for administering the national interest test and call in power, recognising the similar capabilities necessary to support decision making under both tests.

Protection of national security information in court proceedings

[33]

43. **Agree** that the Act should include provisions that preserve the right to natural justice and procedural fairness to the extent possible while protecting national security information in court proceedings, that are broadly aligned with those in existing legislation (such as the Telecommunications (Interception Capability and Security) Act 2013) [33]

Simplifying the regime

Ensuring the investor test focuses on material risks

44. **Note** that the investor test currently imposes compliance costs that are disproportionate to the risks posed by most investors.

45. **Agree** to narrow the investor test and only focus on material risks, by:

45.1. introducing a purpose statement that reflects that the test is intended to assess an investor's character and capability to determine whether they are likely to realise the benefits of their proposed investment, or pose risks to New Zealand

45.2. excluding New Zealanders from the test

45.3. no longer requiring approved investors to satisfy the test after they have already satisfied it, unless there have been relevant changes to their character or capability

45.4. limiting the factors decision makers must consider when assessing an investor's character to whether they have:

45.4.1. been convicted of an offence for which they have been sentenced to imprisonment for a term of five years or more, or, at any time in the preceding ten years, been convicted of an offence for which they have been sentenced to imprisonment for a term of 12 months or more

45.4.2. had any civil contraventions resulting in pecuniary penalties, or entered into any enforceable undertakings, in the preceding 10 years, and

45.4.3. allegations of offences or civil contraventions (for which the maximum penalty is at least equivalent to the penalties referred to in recommendations 45.4.1 and 45.4.2) against them for which official proceedings have commenced

45.5. extending the test to enable consideration of offences and contraventions by, and allegations against, the corporate entity with substantive control over the investment (with offences, contraventions and allegations limited as above), and

45.6. removing the financial commitment criterion and the reference to section 15 of the Immigration Act, and replacing the business experience and acumen criterion with an objective assessment of relevant factors (for example, disqualifications or undischarged bankruptcies).

Benefits test

46. **Note** the current benefits test is unclear, time-consuming to apply, and could better recognise Māori cultural values.

47. **Agree** to simplify and strengthen the benefits test, which will include:

47.1. reducing the number of specific benefit factors while maintaining the range of benefits that can be recognised

47.2. enabling the benefits of protecting wāhi tūpuna, wāhi tapu areas, Māori reservations, and access for the purpose of resource stewardship to be recognised

47.3. clarifying that negative effects of an investment should not be considered under the benefits test (subject to any agreement by Cabinet to recommendation 4848, which would allow assessment of positive or negative impacts on water quality and sustainability, in relation to investments involving water extraction for bottling or in bulk for human consumption)

47.4. clarifying that an investment's benefits should be assessed relative to state of the land and activities on it

47.5. replacing the 'substantial and identifiable' benefit threshold for non-urban land greater than five hectares with a requirement that an investment's benefits should be proportionate to the sensitivity of the land and the interest being acquired in order to satisfy the benefit test, and

47.6. repealing the ability to add factors to the benefits test via regulation.

48. **Agree** that the benefits test, referred to in recommendation 47, in relation to investments involving water extraction for bottling, or in bulk for human consumption, include a factor that allows consideration of the proposal's positive or negative impact on water quality and sustainability.

Timeframes

49. **Note** that the Act does not require decisions on applications to be made within a specified timeframe, creating uncertainty for investors and discouraging investment by contributing to extended decision-making timeframes.

50. **Agree** to introduce timeframes for all decisions to provide greater certainty for investors, which will include:

50.1. enabling specific timeframes to be set via regulation

50.2. providing for the regulator to have an initial period to quality assure an application before statutory timeframes formally commence, and enabling the regulator to charge a fee for this

50.3. enabling the decision-maker to unilaterally extend the statutory timeframe by up to a period prescribed in regulations, or a different period with the applicant's agreement

50.4. ensuring that a breach of a timeframe will not render a decision on an application unlawful and the Crown will not be liable for any loss suffered by applicants, and

50.5. requiring the regulator to report on compliance with statutory timeframes.

Enforcement

51. **Note** that the effectiveness of the regulator's current enforcement tools is limited, and stronger enforcement tools are needed to enable proportionate responses to breaches of the Act and the Regulations, and to manage national security or public order risks.

52. **Agree** to strengthen the regulator's enforcement tools, by:

52.1. enabling it to accept enforceable undertakings and to seek court orders in response to a breach of an undertaking

52.2. increasing the maximum pecuniary penalty for individuals to $500,000 and introduce a separate maximum pecuniary penalty for corporates of $10 million, and introduce pecuniary penalties for a breach of an enforceable undertaking, being $50,000 for an individual and $300,000 for a corporate

52.3. specifying the regulator's ability to seek injunctive relief to address and deter non-compliance, and

52.4. empowering the responsible Minister to seek an Order in Council for managed disposal of an asset or investment when considered necessary to protect New Zealand's national security or public order.

Leases

53. **Note** the Act screens short-term leases, imposing disproportionate costs on investors relative to the risks being managed.

54. **Agree** to extend the threshold for screening leases and other less than freehold interests over sensitive land, excluding residential land, to ten years or more (including rights of renewal), irrespective of whether that threshold is reached in one or more consecutive interests.

55. **Agree** to clarify that periodic leases should not be subject to screening.

Sensitive adjoining land

56. **Note** that the Act screens transactions if the land being acquired adjoins land with sensitive characteristics, but some of this land is screened even though there is no prospect of achieving meaningful access or environmental benefits.

57. **Agree** to limit the screening of sensitive adjoining land to: land adjoining foreshore, bed of a lake, national parks, regional parks if they exceed 80 hectares in area, and land adjoining the following types of land if they exceed 0.4 hectares in area:

57.1. land held for conservation purposes under the Conservation Act 1987

57.2. reserves managed by the Department of Conservation, and

57.3. some land significant to Māori.

Who is required to be screened under the Act

58. **Note** that some entities that most New Zealanders would consider to be fundamentally New Zealand entities, and that are majority owned and controlled by New Zealanders, are deemed to be overseas persons under the Act.

59. **Agree** to amend the definition of overseas persons:

59.1. to remove New Zealand listed and incorporated entities, unless they are either 50% or more owned by overseas persons ('ownership limb'), or where overseas persons holding 10% or more of a class of shares that grants control, cumulatively hold more than 25% of that class ('control limb')

59.2. to remove New Zealand regulated retirement schemes, in which New Zealanders own 75% or more of the assets under management

59.3. to include a managed investment scheme, if the manager is an overseas person, or more than 25% of the scheme's funds are invested on behalf of overseas persons, and

59.4. to increase the control and ownership interest threshold which ordinarily trigger consent requirements under the Act (other than listed bodies corporate) from 25% or more to more than 25%.

60. **Agree** to introduce exemptions from the definition of overseas person that:

60.1. New Zealand incorporated non-listed entities may apply for if overseas persons' control or ownership do not exceed the 'control limb' and 'ownership limb' (recommendation 59.1 refers), and any foreign government or its associates do not hold 10% or more of its shares,

60.2. New Zealand regulated managed investment schemes may apply for, if:

60.2.1. 10% or more of the schemes funds are not invested on behalf of any foreign government or its associates

60.2.2. 50% or more of the funds are not invested on behalf of overseas persons, and

60.2.3. more than 25% of the scheme's funds are not cumulatively invested on behalf of overseas persons that each have 10% or more of the scheme's funds invested on their behalf, and

60.3. in both cases, require Ministers to consider the body corporate or managed investment scheme's compliance with the law and the degree of a foreign government's control before granting an exemption.

When small transactions are subject to screening

61. **Note** the Act screens some smaller, low risk transactions, harming New Zealand's attractiveness to investment particularly in New Zealand's capital markets where smaller transactions are common.

62. **Agree** that overseas persons investing 25% or less of the total equity securities in a New Zealand incorporated and listed entity require consent only if the investment results in the entity breaching the control limb (recommendation 59.1 refers).

63. **Note** the Regulations allow overseas persons that already hold consent to increase their interest by small amounts without obtaining a further consent in certain circumstances.

64. **Agree** to amend the exemption from screening increases in an existing interest to:

64.1. allow the exemption to be used where a 25% or more subsidiary, or 25% or more parent entity, of a consent holder makes incremental increases in an existing interest, or where the overseas person acquired the interest in the asset before it became sensitive;

64.2. remove the requirement that the exemption may only be used within five years of the date of consent, and

64.3. remove the requirement for a consent holder to obtain consent to increase their holding beyond a 90% interest in the relevant entity.

Facilitating trade in residential mortgage obligations

65. **Note** that the Reserve Bank of New Zealand ('RBNZ') has developed a Residential Mortgage Obligation ('RMO'), which is designed to improve banks' and non-bank deposit takers' ('NBDTs') liquidity, but that the Act could serve as a barrier to their uptake because the trades in loans (that is, permitted security arrangements) necessary to support the issuance of RMOs will often require consent.

66. **Agree** to exempt transactions involving the purchase of permitted security arrangements from the Act's consent requirements where:

66.1. the transaction is necessary or desirable to support the issuance or management of RMOs

66.2. the transaction is between a registered bank or NBDT (the loan originator), and a licensed supervisor in respect of debt securities under the Financial Markets Supervisors Act 2011 (the trustee), and

66.3. the transaction is entered into in good faith and in the ordinary course of business.

67. **Note** that new exemptions and amendments to existing exemptions (recommendations 59.4 and 66 refer) will require amendment to the statutory exemption criteria.

Changes to the Fisheries Act

68. **Note** that the Act incorporates the provisions of the Fisheries Act 1996 regulating screening of overseas investment in fishing quota.

69. **Agree** to align the changes agreed to the Act and the Regulations with the relevant overseas investment provisions in the Fisheries Act 1996, including renaming the 'national interest test' in the Fisheries Act 1996, the 'benefit to New Zealand test' and clarifying that the new 'national interest test' (see recommendations 16 and 47) can be applied to prospective investments in fishing quota.

International implications

[36]

[1]

[1]

Review of the Phase Two reform

75. **Note** that I intend to review the:

75.1. proposed call in power three years after its commencement, and

75.2. other Phase Two reform changes five years after their commencement.

Financial implications

[33]

[33]

[1], [33]

[1]

[1], [33]

Legislative drafting

[33]

90. **Invite** the Associate Minister of Finance (Hon Parker) to issue drafting instructions to Parliamentary Counsel Office to give effect to the above proposals by amendments to the Act, the Regulations, the Fisheries Act, the Corporations (Investigation and Management) Act 1989, Conservation Act 1987, the AML/CFT Act and any other legislation requiring amendment as a result of the changes proposed in this Cabinet paper.

91. **Authorise** the Associate Minister of Finance (Hon Parker) to make decisions on:

91.1. proposals to consider tax as part of the screening process in consultation with the Minister of Revenue, the Minister of Finance, the Associate Minister of Finance (Hon Dr Clark), the Minister of Land Information and the Associate Minister of Finance (Hon Jones)

91.2. proposals on which legislation, and agency, should administer riverbed and lakebed; and any other design matters which may arise in relation to the special land provisions during the drafting process, in consultation with the Minister of Land Information and the Minister of Conservation

91.3. proposals to support information sharing between the Act's regulator and other agencies in consultation with Ministers from affected agencies, and

91.4. any additional policy issues that arise during the drafting of the Act and the Regulations.

Authorised for lodgement

Hon David Parker
Associate Minister of Finance

Date:

Appendix 1: Additional detail on proposals to reform the special land provisions of the Act

1. In order to improve the special land (foreshore, seabed, riverbed and lakebed) process, I also propose amending the Act and the Regulations to improve the process via which special land is transferred to the Crown (or in the case of special land that is foreshore or seabed, transferred to the common marine and coastal area under the Marine and Coastal Area (Takutai Moana) Act 2011) so that it works more effectively, including:

    1.1. requiring the Crown to decide within a specified timeframe whether it waives the right to acquire special land

    1.2. specifying the circumstances in which the Crown may waive the right to acquire special land

    1.3. specifying that if the Crown wishes to acquire the special land, it can place a memorial on the title (at which point the special land provisions are satisfied, with a duty on the Crown to take ownership within 10 years or the memorial will lapse)

    1.4. enabling standardised terms and conditions of the transfer of such special land (including, for example, any ongoing access conditions) to be set in the Regulations, which would be mandatory unless the parties agree otherwise

    1.5. specifying that if the Crown does not make a decision on the offer[28] of special land within the current 30 working day timeframe, the offer is deemed to be waived, subject to a duty for the Minister to use his/her best endeavours to make a decision before then

    1.6. clarifying that foreshore and seabed offered to the Crown is transferred to the common marine and coastal area under the Marine and Coastal Area Act 2011, and

    1.7. confirming that the provisions apply only to the acquisition of freehold interests and perpetually renewable leasehold interests under the Crown Pastoral Land Act 1998.

2. The Surveyor-General has also indicated that he is prepared to develop survey standards that adequately define the extent of the private and Crown land, to support the issue of title with less cost and complexity.

28 In practice, an occurs after the parties have reached agreement on the terms and conditions.

Appendix 2: Additional detail on proposed coverage of the national interest test and national security and public order call in power

1. The national interest test is proposed to automatically apply to transactions involving the following high risk critical national infrastructure and strategically important assets:

1.1. significant ports and airports

1.2. electricity generation and distribution businesses

1.3. water infrastructure (broadly, drinking water, waste water, storm water networks and irrigation schemes)

1.4. telecommunications infrastructure

1.5. media entities that have an impact on New Zealand's media plurality

1.6. entities with access to, or control over, dual-use or military technology

1.7. critical direct suppliers to the New Zealand Defence Force, Government Communications Security Bureau and the New Zealand Security Intelligence Service, and

1.8. systemically-important financial institutions and market infrastructure (for example, payments systems).

2. These categories would be specified in regulations.

3. The national security and public order call in power is proposed to cover the same assets (excluding irrigation schemes, recognising that ownership of these assets does not pose national security risks), with the addition of sensitive data [1]

4. Aligning the two tests' coverage is critical to ensuring that it is no easier to purchase an asset covered by the call in power than the national interest test, [1]

5. However, the call in power will differ to the national interest test in some fundamental ways – most notably by applying to transactions not currently subject to screening. It is therefore important to ensure that the call in power is no wider than necessary to avoid imposing undue regulatory burden and ensure that the call in power can be successfully implemented. Accordingly, I propose that:

5.1. asset categories covered by the call in power be prescribed in legislation, but refined and targeted in regulations (rather than wholly specified in regulations), and

5.2. the Minister would need to be satisfied that any regulation is no wider than necessary to manage significant risks to national security or public order and is consistent with New Zealand's international obligations.

6. To provide certainty to investors and ensure that it can be efficiently operationalised, I propose to use the following definitions to determine which entities are in scope of the call in power (with refinements as necessary during the drafting process):

6.1. **media entities** are entities:

6.1.1. where a significant element of the entity's publishing or broadcasting activities, which may include online activities, involves the generation and/or aggregation of news, information and opinion, and

6.1.2. with publications or broadcasts, or online content that have, or will have as a result of a prospective overseas investment, a significant impact on the plurality of news, information and opinion available to:

6.1.2.1. a particular public audience in New Zealand (which for the avoidance of doubt includes limited audiences such as special interest groups or audiences in specific areas or localities in New Zealand), or

6.1.2.2. a particular area or locality of New Zealand.

6.2. Entities that research, develop, produce, or maintain **military and dual-use technologies**, which are:

6.2.1. items listed in Part 1 or 2 of New Zealand's Strategic Good List, and

6.2.2. technologies listed in regulations under the categories of technology that control of, or access to, could pose a significant national security risk.[29]

6.3. Entities listed in a legislative instrument (unless they cannot be listed for security reasons)[30] which **are critical direct suppliers to defence and security services**, where the Minister is satisfied that:

6.3.1. the supplier directly provides critical goods or services to the New Zealand Defence Force, the New Zealand Security Intelligence Service or the Government Communications Security Bureau; and

6.3.2. no alternative suppliers that can be put in place quickly for reasons of the supplier's capability or capacity, or for security reasons.

[33]

30 Critical direct suppliers that are not publicly listed in this instrument will be informed of their status and be required to advise prospective investors of their legal obligations under the power.

6.4. Entities that develop, produce, maintain, or otherwise have access to **sensitive data** that gives rise to significant public order or national security risks, with sensitive data including:

6.4.1. particularly valuable personal information. That is:

6.4.1.1. genetic data

6.4.1.2. biometric data for the purpose of uniquely identifying a natural person

6.4.1.3. data concerning health or a natural person's sex life and/or sexual orientation

6.4.1.4. data about the financial position of a natural person or entity/juridical person, and

6.4.2. official information of the New Zealand Government that is particularly relevant to the maintenance of public order or national security.

Appendix 3: Additional detail on the proposed national security and public order call in power

1. Additional detail on the proposed national security and public order call in power's decision making framework, trigger thresholds for screening are provided below.

2. This appendix also provides more information on the proposed administrative arrangements for the call in power and national interest test.

Decision making framework

3. The call in power would allow the decision making Minister to block or unwind (that is, enforce disposal of) transactions that are found to, or are likely to, present significant risks of harm to New Zealand's national security or public order. To provide investors with additional confidence that the power would not be used capriciously or in circumstances other than those intended, before blocking or unwinding a transaction, the minister would also have regard to:

    3.1. New Zealand's international obligations

    3.2. the extent to which any risks can be mitigated by conditions of consent, and

    3.3. (at the minister's discretion) any potential economic or other benefits associated with the transaction.

4. Requiring consideration of whether conditions could be imposed to reduce risks, or whether there are offsetting benefits, are important mechanisms to help ensure that transactions are not irresponsibly declined.

Trigger thresholds for screening under the call in power

5. An overseas person can potentially gain disproportionate access to, or control over, an asset despite only obtaining a small ownership interest. For this reason, I propose that investments of any size in assets/entities covered by the call in power, except for media entities, be subject to potential review. This reflects the fact that in respect of these assets/entities both access and control risks are relevant.

6. The exception to the criteria in the paragraph above should be investments that result in an investor holding less than 10% of an entity's listed equity securities, unless the investment grants special access to, or control of, that target entity. The Companies Act 1993, Financial Markets Conduct Act 2013, NZX listing rules, and commercial incentives make it extremely unlikely that transactions resulting in small holdings of listed equity securities can pose risks. Further, given the number of trades in listed equity securities each day, including such transactions would create unnecessary uncertainty for industry and investors. For the avoidance of doubt, I propose that any of the following factors would constitute special access to, or control of, the target entity:

    6.1. access to any material non-public information or sensitive data

6.2. membership or observer rights on the board of directors or equivalent governing body, or the right to nominate an individual to a position on the board of directors or equivalent governing body, or

6.3. any involvement, other than through the voting of securities, in substantive decision-making of the business regarding the:

6.3.1. use, development, acquisition, access to, or release of dual-use or military technology or sensitive data;

6.3.2. use of, or access to, high-risk CNI; or

6.3.3. supply of goods or services to the New Zealand Defence Force, Government Communications Security Bureau or the New Zealand Security Intelligence Service.

7. For media entities, I propose that only investments to acquire more than 25% of the entity be potentially subject to the call in power. This is the level at which an investor can obtain 'negative control' over an asset. I recommend this higher threshold for media entities because only control risks are relevant.

The power's notification requirements

8. The call in power's effectiveness will rely, in large part, on the government's ability to detect transactions that are covered by it. I therefore propose that:

8.1. transactions involving dual-use and military technology, and critical direct suppliers to the New Zealand Defence Force and security services be subject to mandatory notification, reflecting that these transactions are more likely to pose risks to national security and/or public order, and

8.2. transactions involving relevant CNI, media entities and sensitive data, reflecting their lower risk profile, be subject to voluntary notification (with investors able to notify the government if they wanted assurance that no action would be taken by the government in respect of that transaction, except, for example, in cases where investors have provided false information or omitted to provide important information).

9. Not requiring notification for low-risk transactions will limit the call in power's regulatory and administrative burden, allowing the regulator to better focus its resources on transactions more likely to present material risks.

Administration of the national interest test and call in power

10. To provide investors and partner jurisdictions with additional confidence that the proposed call in power and national interest test will only be used rarely and best ensure that they are consistent with best practice regulatory design, I propose that:

10.1. the Minister responsible for exercising the call in power and national interest test be a senior Minister and not a Minister ordinarily responsible for decision making under the Act

10.2. this Minister be unable to delegate this power to the regulator

10.3. the Minister be required to publicly report on decisions made under both tests, with exceptions for decisions (or parts of decisions) that must remain confidential to protect national security, New Zealand's international relations, or commercial-in-confidence information

10.4. the Minister's decisions be able to be judicially reviewed (consistent with all other decisions currently made under the Act and comparable regimes globally), and

10.5. the Minister be empowered to publish guidance on the types of matters likely to be considered when determining whether a transaction is contrary to New Zealand's national interest, or security and public order interests, as relevant.

11. To support the Minister in making these decisions, I propose that the regulator be responsible for administering both powers. This reflects the regulator's existing expertise in assessing prospective transactions, its relationships with relevant agencies (including the Government Communications Security Bureau and New Zealand Security Intelligence Service, which will provide advice on potential national security risks), and that using the regulator will retain a single point of entry into, and single agency responsibility for, New Zealand's foreign investment screening regime.

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Appendix 5: Additional detail on proposed changes to the investor test

1. The following changes will ensure the test is more appropriately calibrated to the low level of risk posed by the majority of overseas investors:

    1.1. *Make the purpose of the test clear:* The investor test's purpose is to assess an overseas person's character and capability in order to determine whether they are likely to realise the benefits of their proposed investment, or pose risks to New Zealand.

    1.2. *Target the right investors:* New Zealanders with control of entities that are overseas persons will no longer be subject to the investor test because screening New Zealanders is inconsistent with the Act's purpose. Conversely, the test's scope will be expanded to consider offences and contraventions by corporate entities with substantive control over the investment.

    1.3. Consider only relevant matters:

        1.3.1. Convicted offences for which the overseas person has been sentenced to imprisonment for a term of five years or more, or, at any time in the preceding ten years has been convicted of an offence for which they have been sentenced to imprisonment for a term of twelve months or more. This is consistent with the Immigration Act and is intended to balance the seriousness of offending (for which time of imprisonment is a proxy) with relevance (for which time passed since offending is a proxy)

        1.3.2. Civil contraventions punished by pecuniary penalties, or enforceable undertakings entered into, within the last 10 years

        1.3.3. Allegations (of the same level of offending or contravention) will be able to be considered only where formal proceedings have commenced (though the national interest test could also provide a backstop to scrutinise significant risks where there are no formal proceedings). This goes further than the Immigration Act which does not allow decision-makers to consider allegations when determining residency applications.

        1.3.4. Remove the financial commitment criterion as it is of limited value to the decision-making process. The purpose of this section is not clear given that application costs are high enough to demonstrate financial commitment. No investor has ever been declined on this ground.

        1.3.5. Replace the business experience and acumen criterion with an objective assessment of relevant factors, such as undischarged bankruptcies and disqualifications.

        1.3.6. Streamline the Immigration Act 2009 criterion by removing reference to section 15 of the Immigration Act 2009 (which duplicates the good character criterion), and leaving reference to section 16 of the Act only (which deals with security, public order and public interest matters).

2. I also propose introducing a new power for the regulator to exempt repeat investors from having to satisfy the investor test for each application, unless there have been changes relevant to the investor test criteria since consent.

Appendix 6: Additional detail on proposals to simplify the benefits test

1. I propose to simplify the benefits test in the following ways. I judge that these changes will not reduce the government's ability to manage risks associated with foreign investment, but will generate savings for investors, increasing New Zealand's attractiveness to foreign investment.

    1.1. *Replacing the 21 factors with the following broadly framed factors*:

        1.1.1. an economic benefit factor, supported by a non-exhaustive list of illustrative types of benefits that could be considered (for example, new technologies or skills, increased exports, increased competition, and any reduction in the risk of assets being unable to be sold)

        1.1.2. an environmental factor, related to actual, or likely, benefits on natural and physical resources[31] on the relevant sensitive land or on other land as a result of activities occurring on the relevant land[32], and

        1.1.3. a general public access factor (to replace the existing narrower walking access factor).

    1.2. I also propose to maintain factors relating to:

        1.2.1. historic heritage

        1.2.2. advancing significant government policies

        1.2.3. levels of New Zealanders' involvement in the overseas investment and any relevant overseas person, and

        1.2.4. other consequential benefits.

    1.3. This simplification will maintain the test's scope but make it more straightforward for applicants to address the factors, and the regulator to administer the test. In particular, the broadly framed economic, environmental and public access factors should enable a simpler and more transparent demonstration of benefits, which may now be assessed against the catch-all 'consequential benefits' factor.

    1.4. *Clarifying that the test is positively framed (subject to the alternative option discussed at paragraph 2 below).* This will resolve ambiguity in the Act by clarifying that decision-makers can consider only benefits, rather than the negative effects, against each factor (unless an investment poses significant risks, which would be managed through the proposed national interest test).

    1.5. *Better providing for Māori cultural values*. Consultation with iwi indicated the benefits test could support greater awareness of, and access to, culturally

31 Natural and physical resources would include land, water, air, soil, minerals, and energy, all forms of plants and animals (whether native to New Zealand or introduced), and ecosystems and their constituent parts.

32 Except in respect of fishing quota, where benefits would relate to the relevant investment in fishing quota.

sensitive sites. I propose to do this by clarifying and expanding the benefits test to recognise the benefit of an investor's plans to:

1.5.1. protect or enhance wāhi tūpuna, wāhi tapu, wāhi tapu areas and Māori reservations; and

1.5.2. provide, protect or enhance access across land for the purposes of stewardship of historic heritage or a natural resource. This could include access for particular iwi, hapū and/or marae with a connection to a sensitive site.

1.6. While these changes could involve some additional costs for some investors, this is more than justified by the greater recognition of sites of such cultural importance.

1.7. *Continuing to have no specific reference to water*: I have considered whether to include a factor in the benefits test specifically relating to water bottling or water extraction. I consider that the Act is not the best tool for managing the risks associated with water extraction. The RMA, which applies to all water users rather than just overseas persons, has that role. That is why the Government is proposing a new national direction for essential freshwater, including changes to the RMA to address the problems facing New Zealand's freshwater. Despite this, if Cabinet wishes to expand the Government's ability to consider environmental risks, but do so in a targeted way (refer paragraph 2 of this appendix for detail around a more expansive approach), Cabinet could adopt a targeted factor to address concerns related to water bottling. This factor would allow consideration of any positive or negative effects on water quality and sustainability in respect of proposals to extract water for bottling, or in bulk for human consumption, before granting consent.

1.8. *Simplifying the counterfactual.* I propose a simplified 'before and after' counterfactual test for assessing the level of benefit that will be introduced. Under this revised test, decision-makers will compare the benefits the investor will deliver with the current state of the sensitive land and activity on it. The current counterfactual test, which was put in place by the courts, is philosophically attractive as it seeks to identify the benefits from the overseas investment that are over and above those that would occur anyway. However, its hypothetical nature has made it one of the most complex and time-consuming elements of the Act (anecdotally this doubles the time and cost of applications). My recommendations will make the test less complex, speculative and time consuming.

1.9. *Introducing a proportionality requirement*. I propose explicitly requiring that the benefit of an investment be proportionate to the sensitivity of the land and the interest being acquired (for example, a transaction involving a freehold interest will be more sensitive than one involving a lease). This will apply to all transactions subject to the benefits test. This will codify the OIO's current decision-making approach and replace the substantial and identifiable test, which imposes a higher standard for non-urban land over five hectares but not

other types of particularly sensitive land such as land on offshore islands. Enshrining the rural land directive will retain a higher investment threshold for farmland.

Alternative option: Enhancing the ability to manage environmental risks through the benefit to New Zealand test

2. The version of the benefits test outlined above would only allow Ministers to consider prospective benefits, rather than any negative effects, against each factor (unless an investment posed significant risks, which would be managed through the proposed national interest test).

3. However, there is a high level of public interest and concern regarding how the Act is used to ensure that foreign investment does not pose disproportionately high risks to New Zealand's natural environment. In particular:

3.1. the natural environment is important to many critical sectors of our economy

3.2. New Zealanders place significant value on New Zealand ownership of rural land, and

3.3. the environment is generally significant to New Zealanders' wellbeing.

4. I acknowledge that there are compelling arguments to allow greater consideration of environmental risks when considering overseas investment in New Zealand. I have therefore developed an alternative approach to how environmental matters could be considered under the benefits test.

5. If Cabinet considers that the Act should provide the government with greater capacity to consider such risks, ministers could be able to consider likely or actual environmental harms (of the same types described at paragraph 1.1.2 in respect of environmental benefits) when considering whether to grant consent to applications to acquire non-urban land of greater than five hectares.

6. In completing this assessment, the existence of likely or actual environmental harms would not be – on their own – grounds to deny consent to an investment. Instead, consistent with the proposed operation of the test more broadly, any such harms would have to be weighed against any environmental or other benefits before determining whether the investment was of benefit to New Zealand. To avoid creating undue expectations of the level of analysis required by applicants or the regulator in weighing these factors, it could be made clear that this weighing would be a matter of Ministerial judgement rather than requiring a quantitative calculation.

7. To reduce the possibility of the factor being used to deny consent to applications that only pose limited likely or actual risks of environmental harm, Ministers could be required to consider whether conditions could be imposed on the prospective investment to mitigate, or remediate, any such harms prior to them being weighed as part of the benefits test.

8. For clarity, the counterfactual and proportional approach discussed above in paragraphs 1.8 and 1.9 would also apply when determining the existence, scale, and importance of any actual or likely environmental harms to the determination of whether an investment is, on balance, likely to benefit New Zealand.

9. This approach would best ensure that the factor would operate consistently with the rest of the proposed reforms. However, while it would enhance the government's ability to manage environmental risks, there could also be a number of risks associated with adopting this option. In particular, it could:

    9.1. reduce the Act's coherence, overlap with the role of the national interest test (which is proposed to manage significant risks) and conflict with other legislation that is designed to manage environmental risks;

    9.2. increase the Act's complexity, particularly in the short term, with investors having to provide additional information and the regulator having to complete additional assessments. Given that this proposal would affect between 60% and 75% of applications to acquire sensitive land,[33] this could significantly reduce or even offset any other regulatory savings for applicants;

    9.3. risk inconsistent decision making across different regulatory regimes in respect of similar activities (for example, an application could receive consent under the RMA but be denied consent on environmental grounds under the Act); and

    9.4. increase the chance of overseas investors viewing the balance of the Phase Two reform shifting towards protectionism, rather than reducing red tape, which may reduce New Zealand's attractiveness to foreign investment.

33 Excluding applications to acquire residential land and sensitive land under either of the streamlined forestry tests or intention to reside pathway. This is based on historical analysis conducted to support the development of options to embed the rural land directive in the Act.

Appendix 7: Additional detail on proposals to remove some fundamentally New Zealand entities from the definition of overseas person

1. I propose changing the definition of overseas person so that fundamentally New Zealand entities are not treated as overseas persons and subject to consent requirements, as follows:

    1.1. *Bodies corporate listed on the NZX* will be overseas persons if they are either:

        1.1.1. 50% owned by overseas persons ('ownership limb'), or

        1.1.2. overseas persons holding 10% or more of the listed entities' shares cumulatively control more than 25% ('control limb') - that is, only shareholdings of 10% or more count towards the 25% control limb.

    I propose to count only interests of 10% or more, so only entities with a meaningful amount of overseas control are screened (overseas persons holding less than 10% interest have minimal control). I propose that this definition applies only to listed entities because:

        1.1.3. they are subject to the Financial Markets Conduct Act 2013 and NZX Listing Rules, which reduces the risk posed by investment in those companies; and

        1.1.4. the Act disproportionally affects them because their shareholding changes daily. These daily movements result in listed entities with around 25% overseas ownership or control either pre-emptively applying for consent (although they are yet to reach the 25% threshold) or unintentionally breaching the Act.

    1.2. *Bodies corporate not listed on the NZX* will be able to apply for an exemption if they do not meet the ownership limb or control limb, above, and no foreign government (or their associates) holds 10% or more of the entity's securities. Ministers would also be required to consider:

        1.2.1. the body corporate's compliance record, reflecting that non-listed entities are subject to less regulation than listed entities, and

        1.2.2. the degree of control or access that a foreign Government and its associates may have reflecting that small holdings can result in disproportionate access or control.

    1.3. *Managed investment schemes*[34] will be able to apply for an exemption if any foreign government or its associates does not hold 10% or more of the scheme's value, 50% or more of the value of the scheme is not invested on behalf of overseas persons, and more than 25% of the value of the scheme is not invested on behalf of overseas persons that each have 10% or more of the scheme's value invested on their behalf.

34 Managed investment schemes are a type of registered scheme regulated by the Financial Markets Authority. They pool money from a number of investors and invest on their behalf.

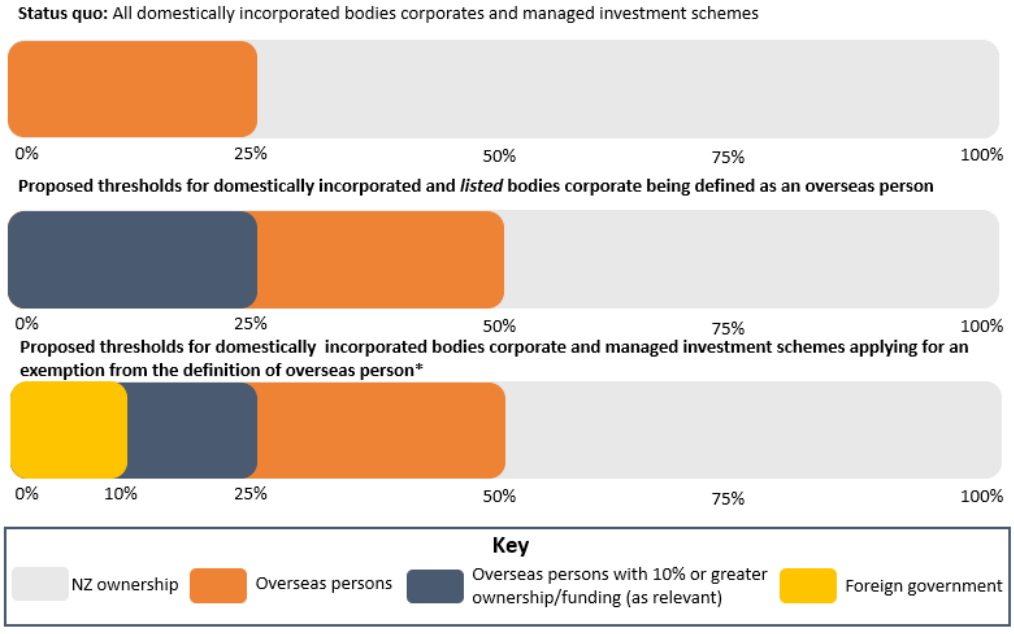
1.4. Similarly, Ministers would consider legal compliance and foreign governments' degree of control or access. To complement the change, I also propose to explicitly include managed investment schemes in the definition of overseas person so that the Act reflects the treatment of these schemes under financial markets law.

1.5. *Retirement schemes in which New Zealanders own 75% or more* of the assets would no longer be overseas persons.[35] This will encourage investment by KiwiSaver and other retirement schemes in New Zealand's capital markets, and improve New Zealanders' long term savings.

2. As part of these changes, I also propose that the general threshold for the definition of overseas person (as it applies to all non-natural persons other than listed bodies corporate) be increased from *25% or more* to *more than 25%*. This is consistent with my proposals above and reflects that an interest of more than 25% is required to exert negative control over an entity.

3. My proposed changes to the definition of overseas person for domestically incorporated bodies corporate and managed investment schemes are depicted in Figure 1.

Figure 1: Proposed changes to the definition of overseas person for bodies corporates and managed investment schemes



*With consideration given to conduct and degree of foreign government ownership (for example, whether a foreign government owner has disproportionately large access or control rights).

35 Currently these retirement schemes are exempt from consent requirements but not the definition of overseas person. This means that retirement schemes that are overseas persons (because, for example, they are managed by an overseas-owned firm) are never required to obtain consent themselves. But they still count as an overseas person when determining whether the companies they invest in are overseas persons. Consent costs associated with that classification reduce returns for New Zealanders.

Appendix 8: Additional detail on proposals to ensure that low risk transactions are not subject to screening

1. I propose making the following changes so that low risk transactions are not subject to screening. This will better ensure that the Act's screening requirements are proportionate to the risks to be managed.

2. These can be categorised into three proposals – no longer screening some transactions that do not grant the overseas person any control, no longer screening some transactions that do not result in an overseas person's degree of control changing, and no longer screening some transactions where the overseas person is not obtaining a real interest in the underlying sensitive assets.

Transactions in listed companies by overseas persons without material control

3. An overseas person (a tipping point investor) requires consent for an investment that results in an entity (that they invest in) that already holds sensitive land or fishing quota becoming an overseas person.[36] As a result, a tipping point investor could be required to satisfy the benefits to New Zealand test even though they may have little to no control over the company they invested in. This issue is particularly problematic for listed companies, which have lots of small shareholdings that can fluctuate daily.

4. I propose changing the rules for tipping point investors in listed companies so that an overseas person only requires consent if, as a result of their investment, overseas persons holding 10% or more across all share classes cumulatively hold more than 25%. This will improve investors' ability to determine when consent is actually required (because there are existing reporting obligations where shareholders hold 5% or more of a class of shares in listed companies) without reducing the government's ability to manage overseas investment.

Smaller transactions, which do not materially change control

5. The Act requires overseas persons to get consent whenever they increase that more than 25% interest. There is an exemption from the requirement to get consent for:

    5.1. increases of 10% or less of the shares held by a consent holder, provided that increase does not go over 'control limits' of 25%, 50%, 75%, 90% or 100% shareholding, and

    5.2. increases of 5% of the shares held by the overseas person (regardless of whether the increase crosses a control limit).[37]

6. The exemption has the technical problems, which limit its application without any reasonable rationale. These are:

    6.1. it only applies to the entity that actually holds the consent so:

36 For example, if a company is 24.9% overseas owned then an overseas person would be required to obtain consent if it purchases the final 0.1% that 'tips' the company into being 25% overseas owned and an 'overseas person' under the Act.

37 Regulation 38 of the Regulations

6.1.1. if a shareholder of a company (A) that holds consent increases its ownership of A by a small amount, the shareholder will not be eligible for the exemption and will be required to obtain consent, and

6.1.2. an overseas person will not be eligible for the exemption and will be required to obtain consent if the asset was acquired before it became sensitive (that is, the original acquisition did not require consent)

6.2. overseas persons are only eligible for the exemption for five years from when they obtained consent, and

6.3. the 90% control limit (which results in screening requirements being imposed on overseas persons increasing their interest over 90%, despite no material change in control).

7. These technical points do not improve the government's ability to manage risk and there is no reasonable basis for them. I therefore recommend amending the Regulations to resolve these technical problems with the exemption so that overseas persons that make small changes in shareholding do not require consent.

Transactions involving interests that do not grant any control over the sensitive asset

8. The Reserve Bank of New Zealand is in the process of developing a new type of debt security called residential mortgage obligations ('RMOs'). In order for a trustee to issue RMOs, the trustee must acquire a parcel of loans (residential mortgages) from a lender. In some circumstances, the lender may also have to purchase these back from the trustee. These loan transfers will often require consent under the Act given that their value is expected to generally exceed $100 million (that is, they will be a 'significant business asset'). There is already an exemption for these types of transactions to the extent that the loans include an interest in sensitive land or fishing quota, but not significant business assets.

9. I propose to exempt transactions connected to the issuance or management of RMOs entered into between banks or non-bank deposit takers, and regulated trustees from screening requirements.