

The Treasury

Reform of the Overseas Investment Act Information Release

May 2020

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- [23] 9(2)(a) - to protect the privacy of natural persons, including deceased people
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Treasury Report: COVID-19 Economic Response: Options to amend the Overseas Investment Act 2005

Date:	6 April 2020	Report No:	T2020/851
		File Number:	IM-5-3-8 (Overseas Investment Act Phase Two)

Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson)	Note the contents of this report.	N/A
Associate Minister of Finance (Hon David Parker)	<p>Note that other jurisdictions have tightened their foreign investment screening regimes in response the changed risk environment presented by the global COVID-19 pandemic.</p> <p>Agree that officials will develop:</p> <ul style="list-style-type: none"> detailed design options for a suite of amendments to supplement the Phase Two reform Bill, which respond to the economic, welfare, and security risks posed by the COVID-19 economic downturn (the 'COVID-19 Overseas Investment Response Bill'), and options for passing a COVID-19 Overseas Investment Response Bill through Parliament. <p>Agree to refer this report to relevant Ministerial colleagues.</p>	8 April 2020

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
[39]	[39]	[39]	N/A (mob) ✓
Thomas Parry	Manager, International	[39]	[23]

Minister's Office actions (if required)

Return the signed report to the Treasury.

Refer the report to: Rt Hon Winston Peters, Minister of Foreign Affairs; Hon Phil Twyford, Minister for Economic Development; Hon Andrew Little, Minister of Justice and Minister Responsible for the GCSB and NZSIS; Hon Dr David Clark, Associate Minister of Finance; Hon Shane Jones, Associate Minister of Finance; Hon James Shaw, Associate Minister of Finance; Hon Damien O'Connor, Minister of Agriculture; Hon Stuart

Nash, Minister of Fisheries and Minister for Small Business; Hon Kris Faafoi, Minister of Commerce and Consumer Affairs; and Hon Eugenie Sage, Minister for Land Information.

Note any feedback on the quality of the report

Enclosure: No

Treasury Report: COVID-19 Economic Response: Options to amend the Overseas Investment Act

Executive Summary

The COVID-19 global pandemic, and related economic downturn, have changed the foreign investment risk environment. In addition to issues with the Overseas Investment Act 2005 (Act) already identified through the Phase Two review (including that the government cannot ensure that investments screened under the Act are in New Zealand's national interest):

- the number of distressed New Zealand firms requiring quick access to equity and debt financing to survive the downturn has, and will continue to, increase. Screening requirements are preventing some transactions vital to firm continuity from proceeding quickly, and
- the value of ordinarily productive firms and strategically important assets are, and will likely continue to, decline below the threshold at which the acquisition of those firms by overseas persons could be scrutinised (generally when they are valued at over \$100 million). This risks overseas persons acquiring assets at 'fire sale' prices with, at the most extreme end, the intention of undermining New Zealand's national security, but also the transfer of welfare-enhancing businesses offshore with a commensurate reduction in domestic living standards.

The same risks are present worldwide. Other jurisdictions (including Australia, Spain, and the European Union) are looking to manage those risks by tightening their screening regimes. You requested advice on options to amend the Act, to protect New Zealand's essential interests.

During the meeting with you on April 1, officials presented high-level options for a suite of supplementary measures to respond to the heightened security and economic risks presented by the COVID-19 pandemic. These would build on the package of changes agreed to by Cabinet under the Phase Two reform, which already go a long way towards enabling the Act to better respond to this current risk environment.

You requested that officials undertake detailed design of options for the supplementary measures, which include:

- temporary measures to strengthen the Act and allow government scrutiny of a wider range of transactions to ensure overseas investment remains consistent with New Zealand's national interest, and
- liberalising measures to remove regulatory barriers to capital flows for firms, and to support New Zealand's economic recovery in the longer term, recognising that our foreign investment screening regime captures many more low-risk and economically valuable transactions than comparable regimes overseas.

While the new liberalising measures are relatively low-risk (for example, an exemption from screening for bank loans above \$100m), there are countervailing risks associated with the introduction of measures to strengthen the Act. Notably, they could have a deterrent effect on overseas investment with implications for New Zealand's longer term economic recovery (though this is somewhat mitigated by other countries having taken similar steps). [34]

Agencies identified further risks with the proposal to enhance scrutiny, including:

- significant operational risks due to the increased transaction volume and potential constraints on the availability of resourcing across agencies, and
- [1]

Reflecting on these likely costs and benefits, on balance we recommend that you agree to the development of policy options to manage COVID-19-related risks as well as options to ensure the urgent passage of any legislation. This would include, as directed by you, an option to implement any changes via a dual track legislative process, under which:

- a time-limited 'COVID-19 Overseas Investment Response Bill' (comprising the full content of the already introduced Phase Two reform Bill and the proposed supplementary powers) is passed under urgency, with a sunset clause, and
- the already-introduced Phase Two reform Bill progresses in parallel on an ordinary legislative track with appropriate Parliamentary and public scrutiny, to take effect on the expiry of the COVID-19 Overseas Investment Response Bill.

It is important that officials work closely with the Parliamentary Counsel Office (PCO) to develop this option, as it would be an unconventional process that departs from existing Parliamentary practice.

We have copied this report to the Minister of Finance for his information.

Next steps

Officials will provide you with further advice on design options for these proposals and for a legislative process on Friday 17 April. We propose that you take a Cabinet paper seeking approval to the suite of supplementary powers and an approach to passing the entire package of amendments to the Cabinet COVID Committee in late April, subject to PCO drafting capacity.

We recommend that you refer this advice to relevant Ministerial colleagues as soon as possible, and initiate discussions about the policy changes and legislative process being considered.

Recommended Action

We recommend that you:

- a **Note** that the COVID-19 global pandemic is expected to place many firms under economic distress, increasing the number of businesses needing quick access to equity and debt financing, and increasing the risk of distressed firms being 'fire sold' to overseas persons without scrutiny.
- b **Note** that other jurisdictions have strengthened their overseas investment screening regimes to respond to the novel economic, security and welfare risks presented by COVID-19 (including reducing screening thresholds to \$0) and New Zealand should consider similar reforms.
- c **Note** that fundamental differences in New Zealand's foreign investment screening regime mean that, in addition to considering liberalising measures that facilitate firms' access to capital flows during the economic downturn and would support New Zealand's economic recovery, it is necessary to consider measures to strengthen the regime.
- d **Agree** that officials will progress:
 - i. detailed design of options to amend the Overseas Investment Act 2005 to respond to the risks posed by the pandemic, which build on the already introduced Overseas Investment Amendment Bill (No 2) (the Phase Two reform Bill), and which together could form a COVID-19 Overseas Investment Response Bill, including options to:
 - i. temporarily empower the government to review transactions worth less than \$100 million which grant investors a degree of control over the target entity,
 - ii. remove consent requirements for low risk transactions that support firms to access capital,
 - iii. manage risks of unintended transitional and operational consequences through new regulation making or exemption powers, and
 - iv. reprioritise the commencement of provisions to ensure that amendments critical to the pandemic response can be operationalised quickly and effectively,
 - ii. in consultation with the Parliamentary Counsel Office, procedural options for urgently passing the COVID-19 Overseas Investment Response Bill through Parliament, while progressing the already introduced Phase Two reform Bill through the ordinary legislative process to ensure appropriate Parliamentary scrutiny.

Agree/disagree.

- e [36]

- f **Note** that there are significant risks associated with these proposals, including:
- i. to the efficiency of New Zealand's economy and attractiveness to investment,
 - ii. to New Zealand's international reputation,
 - iii. that new powers cannot be operationalised as quickly as would be desirable in the current situation,
 - iv. that hastily drafted legislation may have unintended consequences, and
 - v. that the proposed unconventional legislative process is not seen as appropriate.
- g **Note** that mitigations to many of these risks exist (see Appendix D) and that, on balance, we believe that the proposals referenced in recommendation d should proceed.
- h **Agree** to refer this report to the Minister of Foreign Affairs; the Minister for Economic Development; the Minister of Justice and Minister Responsible for the GCSB and NZSIS; all Associate Ministers of Finance; the Minister of Fisheries and Minister for Small Business; the Minister of Agriculture; the Minister of Commerce and Consumer Affairs; and the Minister for Land Information.

Agree/disagree.

Thomas Parry
Manager International

Hon David Parker
Associate Minister of Finance

Treasury Report: COVID-19 Economic Response: Options to amend the Overseas Investment Act

Purpose of Report

1. This report follows a meeting between officials from the Treasury and the Ministry of Foreign Affairs and Trade (MFAT) with you on 1 April 2020. Building on the outcomes of that meeting, this report:
 - provides the Treasury's view on the heightened security and new economic risks posed by foreign investment during the COVID-19-related global economic downturn and the steps that other jurisdictions have taken to manage them,
 - seeks your agreement for Treasury officials, in conjunction with other agencies, to develop for Cabinet's consideration:
 - detailed design options for a suite of supplementary amendments to the Act, which build on the Overseas Investment Amendment Bill (No 2) (the Phase Two reform Bill), to respond to the economic, welfare, and security risks posed by the COVID-19 global pandemic, and
 - procedural options for passing the COVID-19 Overseas Investment Response Bill through Parliament, while also progressing the Phase Two reform Bill on an ordinary legislative track to ensure appropriate Parliamentary scrutiny of the changes, and
 - details potential risks associated with the policy and legislative options being developed and, where they exist, mechanisms to reduce those risks.

Context and problems posed by COVID-19

2. The Act is New Zealand's primary tool for managing foreign investment in New Zealand's sensitive assets.¹ However, the Phase Two reform of the Act revealed a number of flaws that:
 - limit the government's ability to ensure foreign investment is consistent with New Zealand's national interest [1]
 - result in a number of low risk transactions being screened, reducing New Zealand's attractiveness to investment and potentially hampering New Zealand firms' access to the debt and equity capital they need to thrive.
3. On 19 March 2020, the Government introduced the Phase Two reform Bill, which will resolve many of these issues. However, the COVID-19 pandemic has created new risks and revealed additional issues, which the Act would not be well placed to manage without additional legislative reform. In particular, we have identified that:
 - falling firm values caused by the economic downturn increase the risk that overseas persons may be able to acquire,² without any government scrutiny:

¹ The Act screens investments in sensitive land, significant business assets (generally those worth at least \$100 million) and fishing quota. It screens around 15 per cent of foreign investment in New Zealand.

- strategically important assets [1]
 - ordinarily productive businesses important to New Zealand's long-term productivity and economic recovery, and
 - distressed businesses may not be able to quickly enter into a range of low risk debt and equity financing transactions (for example, certain loans valued at over \$100 million). As the Act treats New Zealand's four major banks as overseas persons, lending transactions generally require consent, incurring a delay and cost that could threaten the viability of some firms.
4. Other comparable jurisdictions have already begun to respond to the risks presented by the global pandemic. For example, on Sunday 29 March, Australia announced that it was temporarily lowering the screening threshold for all foreign investments to \$0 to enhance their national and economic security. Spain and the European Union have introduced similar measures (see Appendix E).
 5. Implementing similar temporary measures in New Zealand would introduce new risks. These risks include increasing uncertainty for overseas investors and potentially reducing New Zealand's attractiveness as an overseas investment destination at a time when free flows of capital are particularly critical to our resilience. [36]
 6. On balance, we consider similar legislative reforms in New Zealand to manage these COVID-19 related risks are likely to be justified, provided they were on a temporary basis and managed the aforementioned risks as much as possible.

Proposed solution: Develop a COVID-19 Overseas Investment Response Bill

7. As discussed in the 1 April meeting, to respond to these new and existing economic, welfare, and security risks, we recommend that you direct officials to develop:
 - Policy options to address the new risks posed by the pandemic, to be included in a COVID-19 Overseas Investment Response Bill (in addition to the content of the already introduced Phase two reform Bill):
 - new temporary powers for the duration of the COVID-19 crisis and post-pandemic recovery phase, that allow the government to review transactions worth less than \$100 million that grant investors a degree of control over the target entity,
 - reforms that encourage and facilitate the supply of low risk, high-quality overseas capital critical to business survival and post-pandemic recovery, and
 - amendments to exemption and regulation making powers, as well as to the commencement timing of certain provisions, to support the implementation of the broader package.

We note that expanding the Act's coverage without also liberalising low risk capital flows would pose potentially material risks to New Zealand's economy. Appendix B includes additional detail on these proposed measures.

² For example, as of 3 April 2020, the NZX50 had fallen nearly 20 per cent below its February 21 peak. Many unlisted entities and entities in particularly exposed sectors (such as tourism) will have suffered greater falls.

- A process for urgently passing the COVID-19 Overseas Investment Response Bill, while progressing the Phase Two reform Bill on an ordinary legislative track, to ensure that the changes in the latter Bill are credibly reviewed by the Parliament and the public before coming into long-term effect.
 - In short, this could involve passing the COVID-19 Overseas Investment Response Bill under urgency and time-limited by a sunset clause, while referring the Phase Two reform Bill (as introduced) to Select Committee for review. It would then be for Parliament and the Government to work together to finalise passage of the Phase Two reform Bill through the House before the COVID-19 Overseas Investment Response Bill sunsets.

While there are benefits to this dual track approach it is not without risks (detailed below and at Appendix C). We will work with the PCO and other agencies as relevant to identify these, and mitigate them where possible. We will also consider whether alternative procedural options exist to achieve the government's objectives that would be more consistent with ordinary Parliamentary procedures.

8. We will consult with officials from relevant agencies, including MFAT, PCO, and the Overseas Investment Office (OIO) to develop this advice.

Risks

9. We consider that the proposed urgent passage of a COVID-19 Overseas Investment Response Bill to respond to COVID-19 related foreign investment risks and economic pressures has significant merit. However, the proposal also presents significant risks. These could be closely considered in the detailed design of the response measures, including:
 - that the screening of larger volumes of transactions unintentionally slows or prevents the consenting of critical transactions that are essential to firm viability during the pandemic, and to facilitating economic activity in the recovery phase,
 - reducing New Zealand's attractiveness to overseas investment,
 - [1]
 - significant operational risks, relating to:
 - the rapid establishment of a new screening mechanism and associated processes (such as guidance, information sharing protocols, and governance arrangements), and
 - expected delays in the processing of transactions ordinarily subject to consent,
 - that because the COVID-19 Overseas Investment Response Bill will not have the benefit of Select Committee scrutiny, the new provisions may have unintended consequences or not operate as intended,

- that use of an unconventional process for passage of the COVID-19 Overseas Investment Response Bill (one prohibited under Standing Order 264)³ will be seen as inconsistent with constitutional norms, in turn undermining the Bill's credibility and potentially raising questions about the Government's commitment to Parliamentary scrutiny.
10. Agencies have identified mitigations for many of these risks, and we would work with the relevant agencies (OIO, PCO, [1], and others) to implement them. However, even with mitigants in place, significant risks would remain (see Appendix D for additional information).

[1,36]

Next Steps

14. If you agree to the recommendations in this report, officials will develop the policy and process options outlined above for your consideration.
15. We will provide you with further advice on these matters by Friday 17 April, and seek your approval (as Attorney-General) to engage with PCO to draft a COVID-19 Overseas Investment Response Bill.

³ This Standing Order prevents a Bill that is the same in substance as a bill that received, or was defeated on, a first, second or third reading; or an amendment to the Bill that is the same in substance that as agreed to or defeated in a committee of the whole House being proposed in the same calendar year. The Business Committee could waive this Standing Order, however we note there may be risks in relying on securing this waiver to progress the COVID-19 Overseas Investment Response Bill.

16. The Cabinet COVID Committee (or other appropriate committee) could jointly consider a COVID-19 Overseas Investment Response Bill and Cabinet paper seeking authority to the proposed policy changes by late-April 2020, subject to PCO resourcing. The COVID-19 Overseas Investment Response Bill could then be introduced to Parliament in early-May 2020, if Parliament has resumed by that time.
17. Given the significance of these proposals, the unconventional Parliamentary process, and the urgency underlying the entire package, we recommend that you refer this report to the following Ministers: the Minister of Foreign Affairs; the Minister for Economic Development; the Minister of Justice and Minister Responsible for the GCSB and NZSIS; all Associate Ministers of Finance; the Minister of Fisheries and Minister for Small Business; the Minister of Agriculture; the Minister of Commerce and Consumer Affairs; and the Minister for Land Information.

Consultation

18. We consulted with MFAT, OIO, Land Information New Zealand, PCO, the Ministry of Business, Innovation and Employment, the Department of Prime Minister and Cabinet, the NZSIS, the GCSB, New Zealand Trade and Enterprise, the Ministry for Primary Industries, and the Ministry of Justice, to produce this report.

Appendix A: Additional detail on the economic and security risks posed by COVID-19

19. The COVID-19 pandemic has created new risks and revealed additional issues with New Zealand's foreign investment screening regime that could affect New Zealand's economic and security interests. These are detailed below.

Economic and security risks associated with foreign investment during the COVID-19 pandemic

20. The threat posed by COVID-19 and measures taken by governments worldwide to restrict public transmission are having significant negative effects on the global economy, with the value of many businesses falling precipitously (particularly in exposed sectors, such as tourism).
21. Declining firm values are increasing the risks posed by foreign investment. This is because most jurisdictions, including New Zealand, only screen investments above a certain dollar threshold (for example, New Zealand generally only screens investments in business assets worth at least \$100 million).⁴ The current economic may cause the value of many economically important businesses to fall below this threshold. This increases the chance that the following transactions could occur without any opportunity for government scrutiny:
- [1]
 - overseas persons acquiring productive businesses with special brand value, valuable international connections, or sensitive intellectual property, resulting in a transfer of wealth offshore to the detriment of long term domestic welfare and living standards.
22. We believe that there are strong grounds for New Zealand to consider strengthening measures similar to those being pursued overseas (see Appendix E), as well as urgently bringing forward the Phase Two reform Bill to protect New Zealand's essential interests. However, it is critical that these are accompanied by liberalising measures that facilitate essential capital flows to support New Zealand's economy.

COVID-19 pandemic has revealed additional issues with the Act that limit access to capital

23. The global pandemic is already placing a number of New Zealand businesses under financial stress. While measures taken by the Government to date are reducing these pressures, we expect many productive New Zealand businesses to need additional debt and equity capital to survive this downturn and, critically, to recover and grow in the aftermath.
24. Unfortunately, the Act is distinct from almost all other foreign investment screening regimes, as it:
- requires many low risk transactions providing debt financing or equity injections to obtain consent,
 - treats more domestically incorporated and owned entities as overseas persons, with subsequent consent requirements creating barriers to domestic mergers and acquisitions, and

⁴ In New Zealand, this figure is generally \$100 million, though can be higher for investors from countries that New Zealand has free trade agreements with. For example, the threshold for non-government Australian investors is \$537 million.

- treats New Zealand's largest banks as overseas persons, obliging them to seek consent to provide credit and enter transactions to manage their own risk portfolio. This is not the case in countries with locally owned banking sectors and deeper domestic capital markets.
25. The Phase Two reform Bill and agreed changes to the Overseas Investment Regulations 2005 (the Regulations) will go a long way towards resolving many of these issues. However, market participants have raised concerns that the Phase Two reform Bill does not deal with the consent requirements for certain other types of loans and securitisation transactions, in effect limiting their ability lend to firms. If unaddressed, these barriers risk increasing the number of firms that are forced into overseas ownership during the pandemic because the processes for obtaining lending from a bank versus an injection of overseas equity are the same under the Act.
 26. Consequently, we believe that it is necessary to bring forward and develop new tools to facilitate low-risk capital flows and support New Zealand businesses, in conjunction with bringing forward existing, and developing new, powers to manage foreign investment risks.

Appendix B: Overview of proposed supplementary policy changes

27. This Appendix details proposed measures to supplement the changes contained in the Phase Two reform Bill, needed to respond to the risks posed by:
- the global COVID-19 pandemic, and
 - urgently passing a rapidly-prepared and complex COVID-19 Overseas Investment Response Bill, without normal Parliamentary or public scrutiny.

New powers to manage risks posed by transactions worth less than \$100 million

28. As detailed above, the pandemic presents significant risks in relation to foreign investment in businesses worth less than \$100 million.
29. To respond to these unprecedented risks, we are considering the design of a temporary emergency power that would allow the government to review transactions worth less than \$100 million (where they result in the acquisition of 25 per cent or more interest by an overseas person).⁵ This power would be time-limited and include a provision requiring periodic reviews to test that the power remained necessary. At a high level, this power could:
- require investors to notify the government of any transaction below \$100 million, and
 - empower the Minister to:
 - i allow no or low risk transactions to proceed quickly, without intensive review (recognising that delays could threaten business viability), and
 - ii impose conditions on, block, or unwind transactions considered contrary to the national interest.⁶
30. To simplify the drafting process and improve investors' understanding of the new power, officials will design the power by drawing on concepts already contained in the Act and Phase Two reform Bill. We will also consider how this power would interact with other work being developed across the Treasury to support large and complex entities during this economic downturn.
31. Where the government has made a decision about a transaction, the Act currently prevents the government from taking future action in relation to that transaction, unless the investor relied on, for example, false and misleading information.

New exemptions to support firms' access to finance

32. To ensure that firms can access debt and equity capital, we are considering whether it would be appropriate to exempt certain low risk transactions from consent requirements. These measures could facilitate capital flows to New Zealand businesses during the crisis, and bolster their growth and recovery after the pandemic. We have identified the following options.
- *Exemption for loans by banks in excess of \$100 million:* currently registered banks and licenced non-bank deposit takers that are overseas persons (which includes the four major banks) must get consent to lend more than \$100 million.

⁵ This is consistent with the Act's general threshold for consent for indirect investments.

⁶ Consistent with the current Act, we consider that transactions would only be able to be 'unwound' (that is, disposal ordered) where there has been a breach of the Act – for example, the investor did not notify their transaction, obtained their 'no action' notice using misleading information, or breached ongoing conditions of consent.

- *Sale of securitised loans*: currently the purchase of more than \$100 million in securitised loans by an overseas person requires consent. This limits banks' and other creditors' ability to manage their balance sheet and diversify portfolio risk across the economy. This can mean such firms are less willing to lend to the real economy.
33. Unlike the proposed new power to screen transactions below the \$100 million threshold, we do not envision that these exemptions would be temporary. While the current economic situation has revealed and amplified the need for the exemptions, our initial view is that they should become a long-term feature of New Zealand's screening regime.

New powers to manage transitional risks

34. There will be risks arising from the rapid roll-out and implementation of a COVID-19 Overseas Investment Response Bill. The risks include, but are not limited to, capturing classes of low risk transactions, and that some provisions do not operate as expected. We anticipate these risks because of the speed at which the COVID-19 Overseas Investment Response Bill would be drafted and because it will not have the benefit of Select Committee scrutiny.
35. We consider that the following new powers may be required to manage these and related risks:
- an exemption making power, potentially vested with the Minister responsible for the Act (the Minister of Finance), rather than permitting exemptions to be made through regulation as is ordinarily the case, and
 - a regulation making power, that would enable regulations to be used to amend the Act. The New Zealand government has used similar powers to respond to previous crises, including the Canterbury and Kaikoura earthquakes. They may be necessary in this case to manage transitional and implementation risks.

[36]

Changes to the timing of commencement for other provisions/regulations

36. To ensure that the government has the powers and operational capacity it needs to manage economic and security risks posed by the pandemic as quickly as possible, consideration will be given to:
- bringing forward the introduction of the national interest test under the COVID-19 Overseas Investment Response Bill, to ensure that the Government can block investments that are contrary to New Zealand's national interest as soon as possible (under the Phase Two reform Bill, this mechanism would not commence until around 6 months after that Bill receives Royal Assent),
 - bringing forward the commencement of several previously agreed exemptions that facilitate firms to access debt and equity capital (such as exemptions for adjustments of existing shareholdings and exemptions for corporate restructuring where ultimate control does not change), to support firm viability, and

- delaying other provisions of the COVID-19 Overseas Investment Response Bill that are less critical to manage the risks presented by the pandemic, and to ensure that the OIO and other affected agencies can concentrate their limited resources on implementing and operationalising critical features of the reform (such as the proposed screening power for transactions worth less than \$100 million).

Appendix C: Process for urgent passage of a COVID-19 Overseas Investment Response Bill

37. As discussed above, the escalating security and economic risks caused by the COVID-19 situation mean that amendments to the Act are time-sensitive. Officials believe that the existing and new problems with the Act should be resolved urgently to protect living standards during the crisis, and support the subsequent economic recovery.
38. Notwithstanding this relative urgency, it will be important to ensure that any amendments to the Act are subject to appropriate Parliamentary and public scrutiny. This was true for the Phase Two reform Bill as introduced, given its complexity and the compressed time period available for drafting. The supplementary amendments that respond to COVID-19 risks only increase this need. It is therefore critical that these reforms be subject to a credible Select Committee process.
39. Consistent with discussions with you during the 1 April meeting, we propose to develop, in consultation with PCO, an option for implementing these reforms that could include:
- the introduction and passage (under urgency) of the COVID-19 Overseas Investment Response Bill. This Bill would not be referred to Select Committee and would include a sunset clause triggering its expiry after a fixed period, and
 - the first reading and referral of the already-introduced Phase Two reform Bill to the relevant Select Committee for review. It would then be contingent on the Government and the Committee to work together to ensure that this Bill can be reported back and passed through Parliament before the COVID-19 Overseas Investment Response Bill expires.
40. This would be an unconventional process, which runs counter to Parliamentary practice and Standing Orders; the process is prohibited under Standing Order 264. It would involve far more transitional complexity and uncertainty for investors, the regulator, and New Zealanders than would ordinarily be the case. It may undermine Parliament's role in the scrutiny and refinement of legislation and duplicate Parliament's processes.
41. As the Phase Two reform Bill was prepared on a relatively short timeframe, there is a heightened risk that, without a Select Committee process, the COVID-19 Overseas Investment Response Bill's provisions do not work as intended, leading to uncertainty and legal risk for investors and New Zealanders seeking overseas investment. These risks would be amplified for the supplementary provisions in the COVID-19 Overseas Investment Response Bill.
42. However, under the circumstances, we consider that the dual track process offers a potential way to ensure that necessary reforms are implemented as quickly as possible while providing a backstop that ensures the substance of the Phase Two reforms are subject to appropriate scrutiny. This would be dependent on the Cabinet Business Committee waiving the Standing Order requirements. Some residual risks could also be managed, or at least better understood by engaging:
- the Business Committee, on the potential breach of Standing Orders, and
 - Parliament's Office of the Clerk, on the potential dual track process more broadly.
43. [36]

[36]

44. We note that while the options presented by PCO are less risky, pursuing those options would likely involve trade-offs against other reform objectives, such as limiting how urgently the reform package could be put in place.
45. Parliament is currently adjourned, but is due to resume on April 28 (subject to the country's COVID-19 alert level at that time).

Appendix D: Risks associated with a COVID-19 Overseas Investment Response Bill proposed measures and process

46. There are a number of risks associated with this proposal, which are detailed below. While many of these can be mitigated, others cannot. Where mitigations exist, they have been described.

Risk that a lower investment screening threshold slows critical transactions

47. Any reduction in New Zealand's screening threshold would inevitably increase the number of transactions subject to screening (though it is not possible to estimate volumes at this time). Even with additional exemptions for low risk transactions in place, many of the transaction captured by a lower threshold would nonetheless be low risk. They will also be of increasing importance to business viability. Regulatory delays caused by this screening requirement could impose real costs on the economy.
48. Officials will endeavour to design a screening mechanism that allows for such low risk transactions to proceed quickly. However, the ability for these transactions to be pushed through the system will be constrained by the OIO's resource capacity, readiness to operationalise changes across the system, and Ministers' risk tolerance (that is, a risk averse approach will increase the chance that the reforms overly limit economic efficiency). If the Act's screening threshold is lowered, it will be imperative that Ministers:
- actively engage with the OIO to explain their risk tolerance and the types of transactions that they are particularly concerned about,
 - [33]
 - [1]

Risk of reduced investment attractiveness and to New Zealand's international reputation

49. There is a risk the introduction of a COVID-19 Overseas Investment Response Bill with the proposed new power to screen investments below the Act's current \$100 million threshold could reduce New Zealand's attractiveness to investment. This could occur as a result of:
- the expansion in the number of transactions requiring screening,
 - reduced certainty and understanding for investors and their advisors given a lack of familiarity with the new tests, and

[1]

51. It would be possible to reduce these risks by:

- emphasising that New Zealand's changes are based on similar actions taken in a number of other comparable jurisdictions (meaning that investments in those jurisdictions would similarly be subject to new and additional review periods),
- ensuring that the COVID-19 Overseas Investment Response Bill includes supplementary measures to carve out low risk transactions,
- ensuring that the COVID-19 Overseas Investment Response Bill is time-limited, to be replaced by the Phase Two reform Bill which will have been fully considered by Parliament,
- emphasising that the COVID-19 related tools are temporary (with the exception of the liberalising measures), tied to the duration of the COVID-19 crisis, and their appropriateness to the current situation would be subject to regular review,
- deliberate and proactive engagement with key international partners on the rationale for the COVID-19 related tools and emphasis of their temporary time-bound nature,
- engagement by MFAT and New Zealand Trade and Enterprise in foreign markets to make clear that New Zealand remains open to productive, sustainable and inclusive investment, and
- preparing a comprehensive communications package for domestic and international audiences that provides clear guidance on the COVID-19 Overseas Investment Response Bill's purpose, how its provisions operate, how future regulations are expected to operate (where this is known), and the Government's view on what types of transactions may raise national interest concerns.

Operational risks

52. Currently New Zealand's foreign investment screening regime does not include a national interest test. [1]
53. Bringing forward and expanding the scope of the national interest test (or a similar test for transactions of less than \$100 million) would require the OIO to urgently develop new forms, guidance, information sharing, and cross-agency governance systems, and potentially to hire additional staff, in an environment where most workers would likely be working remotely.
54. This poses a significant risk of the OIO being unable to complete all of its business as usual work while still meeting its Key Performance Indicators. This could mean, for example, that less economically critical transactions take longer to get consent than they ordinarily would.
55. [1]

Drafting risks

56. There is a heightened risk that, if the COVID-19 Overseas Investment Response Bill does not have the benefit of a Select Committee process, the provisions from the Phase Two reform Bill and the new supplementary provisions have unintended consequences or, in the worst case scenario, do not operate as intended. This would undermine the credibility of New Zealand's screening regime and, depending on how any errors manifested, could impose real costs on the economy.
57. PCO has significant resource constraints as it working on the Government's broader COVID-19 response package. This means that it may take longer to prepare the supplementary COVID-19 response measures than would ordinarily be the case.
58. These risks could be partially mitigated through inclusion of new, temporary, exemption and regulation making powers in the COVID-19 Overseas Investment Response Bill (see Appendix B). However, these kinds of tools would likely raise concerns around the appropriateness of the exercise as a whole, as they will affect the legitimacy, durability, predictability, and transparency of the law.

Process risks

59. There are significant risks associated with passing a COVID-19 Overseas Investment Response Bill, as proposed, under urgency. Among other things, urgency can used:
 - to enact a government policy without the delay of a legislative process, or
 - in circumstances of urgent need, for immediate fixes that respond in a proportionate way to the immediate problem.
60. PCO advise that the second purpose is seen as more constitutionally valid. Consequently, while it may be justifiable to bring forward elements of the Phase Two reform Bill and new supplementary powers to manage COVID-19-related risks, it is harder to justify using urgency to bring forward the elements of the Phase Two reform that do not respond to such risks (for example, changes to farmland advertising requirements). There is a risk that this may undermine the COVID-19 Overseas Investment Response Bill's credibility and could raise questions about the Government's commitment to Parliamentary scrutiny.
61. This argument has significant merit. We note, however, that the vast majority of the COVID-19 Overseas Investment Response Bill would implement measures that either enhance the government's ability to manage relevant risks, or liberalise low risk capital flows. While some measures would not meet this criteria, it is not clear that it is necessary to split the Bill into different parts, given that:
 - among the most substantial of these non-COVID response measures, new consent requirements for the acquisition of farmland, simply legislate for the status quo under the Ministerial Directive Letter, and
 - splitting the Bill would increase complexity for PCO, the Treasury, the Parliament, and other stakeholders relative to a Bill that includes all the relevant changes.

Appendix E: Additional detail on changes internationally to manage COVID-19-related risks

62. A number of jurisdictions have taken steps to manage the economic and national security risks posed by the COVID-19-related economic downturn. These are outlined below.

Australia

63. Australia has temporarily reduced the screening threshold for all overseas investments in land and business to \$0, and extended the timeframe for assessing applications from 30 days to six months. Critically, while dropping the threshold to \$0, they have retained the existing threshold for screening at 20 per cent. This means that the acquisition of a 20 per cent or greater interest by an overseas person in a company of any value will be assessed to determine whether it is contrary to Australia's national interest.

64. [2]

65. [2]

Spain

66. On 18 March, Spain responded to the COVID-19 pandemic by temporarily amending their regime to require ex-ante approval for foreign (non-EU) direct investments, including those by foreign state actors, in strategic sectors in Spain that result in:
- the acquisition of a 10 per cent or greater interest in a Spanish company, or
 - the foreign investor having effective participation in the management or control of a foreign company.

The European Union (EU)

67. On 25 March, the European Commission published guidelines to EU Member States calling on them to adopt or strenuously enforce their foreign investment screening mechanisms to protect sensitive assets from foreign takeover during the crisis. The Commission urged Member States to make full use all powers available to protect Europe's security and public order.