

The Treasury

Phase 2 Reform of Overseas Investment Act Information Release

March 2021

This document has been proactively released by the Treasury on the Treasury website at

<https://www.treasury.govt.nz/publications/information-release/phase-2-overseas-investment-act-reform>

Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

- [1] 6(a) - to avoid prejudice to the security or defence of New Zealand or the international relations of the government
- [2] 6(b)(i) - to avoid prejudice the entrusting of information to the Government of New Zealand on a basis of confidence by the Government of any other country or any agency of such a Government
- [25] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information
- [31] 9(2)(f)(ii) - to maintain the current constitutional conventions protecting collective and individual ministerial responsibility
- [33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
- [34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
- [35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment
- [36] 9(2)(h) - to maintain legal professional privilege
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [39] appearing where information has been withheld in a release document refers to section 9(2)(k).

Copyright and Licensing

Cabinet material and advice to Ministers from the Treasury and other public service departments are © **Crown copyright** but are licensed for re-use under **Creative Commons Attribution 4.0 International (CC BY 4.0)** [<https://creativecommons.org/licenses/by/4.0/>].

For material created by other parties, copyright is held by them and they must be consulted on the licensing terms that they apply to their material.

Accessibility

The Treasury can provide an alternate HTML version of this material if requested. Please cite this document's title or PDF file name when you email a request to information@treasury.govt.nz.

Reference: T2020/1314 IM-5-3-8-9

Date: 5 May 2020

To: Minister of Finance (Hon Grant Robertson)
Associate Minister of Finance (Hon David Parker)

Deadline: 6 May 2020 (for DEV)
(if any)

Aide Memoire: Economic Response: Reform of the Overseas Investment Act 2005 – talking points for DEV

Purpose

On 6 May 2020, Cabinet's Economic Development Committee is scheduled to consider a Cabinet paper and two draft Bills relating to a proposed new suite of reforms to the Overseas Investment Act 2005 ('Act'). This Aide Memoire provides key messages to support discussions and 'back-pocket' talking points about the specific proposals.

Suggested talking points

- The Act provides the framework for regulating foreign investment in New Zealand's sensitive assets. In the Phase Two reform Cabinet recently agreed to changes to strengthen the government's ability to manage high risk foreign investment and reduce unnecessary red tape.
- Key changes from the Phase Two reform include the introduction of a national interest test, and the removal of fundamentally New Zealand entities (such as listed companies) from screening. A Bill to give effect to these changes was introduced to Parliament on 19 March 2020, and is to be withdrawn ahead of the introduction of the two draft Bills.
- The global COVID-19 pandemic and the related economic downturn have changed the foreign investment risk environment, both here and across the world. Other countries, such as Australia, have already taken steps to increase government visibility of foreign investment.
- In New Zealand, these conditions have intensified issues with the Act that were identified in the Phase Two reform, and also revealed some additional issues. These are resulting in:
 - an increased risk that productive businesses that make valuable contributions to New Zealanders' wellbeing but which are experiencing financial distress could be sold to foreign investors at depressed prices without government scrutiny, and
 - an increasing number of economically distressed firms requiring debt and equity finance to remain viable. These kinds of financing transactions tend

to require consent, which causes delays to the flow of capital can compromise a firm's survival.

- Although the fiscal support measures in the Government's business package will cushion the negative economic impacts of the pandemic for many businesses, that financial support is unlikely to be sufficient. Some firms will need access to external foreign capital to remain viable.
- Foreign investment will be vital to our economic resilience while the pandemic continues, and then to our growth in the aftermath. This means it is critical the government is able to manage the risks associated with such transactions, but equally that intervention does not delay investment that protects jobs and economic growth.
- I propose introducing three new investment screening tools, to enable the government to manage the heightened foreign investment risks. These build on aspects of the Phase Two reform, which have been combined in the Emergency Measures Bill. The proposed new tools to manage the pandemic-related foreign investment risks are:
 - a temporary emergency notification power requiring investors to notify all foreign investment transactions (regardless of monetary value) that will grant control over a business or its assets, which can then be screened for consistency with the national interest,
 - no longer screening two low risk classes of transactions that facilitate lending by banks and portfolio management, and
 - introducing new regulation making powers to manage the transitional risks associated with the rapid development and implementation of these proposals.

[1,36]

- These reforms will increase the number of transactions subject to review. To avoid creating delays I have agreed to statutory timeframes whereby there will be an initial 10 days to assess a notification and assess if it needs detailed review. Most investments will be quickly triaged out of the process. A further 30 days is then available to undertake a national interest assessment if needed.
- These reforms are needed urgently to protect New Zealand's essential interests. I've proposed implementing the reforms through a 'split bill' legislative process which involves:
 - introducing the (tabled) Emergency Measures Bill under urgency, referring it for FEC consideration and report back in time for it to complete its second and third readings and be passed under urgency in the week of 25 May. This Emergency Measures Bill is made up of the three new investment screening tools and some changes from the Phase Two Reform which are critical to the Government's COVID-19 response, and

- the remaining Phase Two changes are introduced in the (tabled) Other Measures Bill. This is introduced concurrently with the Emergency Measures Bill, but is referred to the FEC to follow an ordinary legislative track.
- It's important that the enduring changes in the Emergency Measures Bill are subject to appropriate scrutiny, so I've proposed that the Select Committee be given scope to consider the enduring provisions of the Emergency Measures Bill and recommend any changes when they review the Other Measures Bill. This would be after the Emergency Measures Bill has been passed under urgency.

Annex 1: Back-pocket talking points

What is the role of this overseas investment reform in the broader economic response?

- These proposals form part of the Government's COVID-19 economic response. They will help to secure and support the business sector and manage foreign investment risks, supporting New Zealanders' wellbeing.
- It is important the new investment notification power needs to work in tandem with the range of business support policies in the economic response package.
- The new investment screening tools have been designed to be consistent with:
 - existing COVID-19 response policies such as the wage subsidy, support for SMEs and easing of insolvency requirements (which lower the likelihood of New Zealand businesses needing to rely on foreign investment), and
 - the criteria that define 'Economically Significant Businesses' which the Crown uses to consider whether to provide financial support to distressed businesses (this ensures the Crown's approach to interventions in the economy is consistent).

What is involved in the emergency notification regime for all investments in existing businesses and business assets?

- The proposed emergency notification regime would require overseas persons to notify the government of any controlling investment in an existing business or certain business assets, that wouldn't ordinarily require consent. This applies to:
 - investments of any value in existing businesses that acquire a more than 25 per cent interest, or increase an existing holding to or beyond a 50, 75 or 100 per cent interest,
 - investments of any value in business assets that result in a more than 25 per cent acquisition of the total value of a New Zealand business' assets.
- Notified transactions will be reviewed to determine whether they can proceed quickly, or require an assessment against the national interest. If a transaction is found to be contrary to the national interest, the Minister could impose conditions, block or unwind the transaction.
- The notification process for investors will involve completing a short and easy to fill-in form with details of the proposed transaction.
- The power would be reviewed every 90 days and removed when the pandemic or its economic aftermath are no longer having a significant impact in New Zealand.
- To manage the burden imposed on lower risk transactions captured under this power, I have proposed that Cabinet agree to:
 - a non-exhaustive list of national interest risk factors that will support the initial triaging of applications, and
 - issue public interest on the matters that will always be considered in a national interest assessment.

What transactions will no longer require consent?

- Cabinet agreed to a range of liberalising measures for low risk transactions in Phase Two. These include reducing the scope of what is sensitive land, and narrowing the definition of an overseas person.
- I have recommended that two further classes of transactions, which facilitate banks to lend and manage risk across the economy, be exempt from the Act. These are:
 - the issuance of loans by registered banks, and
 - the acquisition of parcels of securitised loans by overseas persons.
- Both are low risk transactions, as they do not confer an interest in the underlying sensitive asset, only in the revenue flows generated by the firm. Residual risks can also be managed through statutory constraints and limiting the lending exemption to prudentially-regulated financial institutions.

What are the regulation making powers?

- These proposals have been developed rapidly, in line with escalating risk environment. [34]
- There are risks that the emergency notification power captures an unintentionally broad range of transactions, and/or that transitional issues or errors result from the drafting.
- The three regulation making powers would enable the Minister to recommend exemptions for a variety of transactions, to amend consent requirements for classes of transactions, and to modify provisions of the Act if needed for its orderly implementation.
- These powers would be repealed by the Other Measures Bill as there is not a permanent need for them.

How will the proposals affect the treatment of assets already screened? [31]

- This will not change the treatment of assets already screened under the Act, such as investments in farmland.
- I do not expect that the exemption making power would be used to establish exemptions for a wide range of transactions beyond the lending transactions identified in this paper.

Has the Government considered using the NZ Superfund to provide financial support to businesses that might otherwise seek foreign capital? [31]

- The government issue general directions to Guardians of the New Zealand Superannuation Fund relating to the Fund's performance, however these cannot be inconsistent with the Fund's statutory obligations around management and administration.
- This means the Minister of Finance cannot issue a direction to the Fund to make particular investments.

Annex 2: Actions taken by other jurisdictions

What actions have been taken by other jurisdictions?

- New Zealand is not alone in taking measures to increase oversight of foreign investment in the current crisis. Australia, Canada and a range of European countries have all tightened their ability to review transactions, through similar measures to those I have proposed.

Australia

- In late March, Australia announced a temporary lowering of all monetary screening thresholds to \$0. This applies to all foreign investments in business and land that grant a foreign investor a 20 per cent or greater interest in a company (the current control threshold).
- Foreign investors must notify eligible transactions to the Treasurer for review to ensure they are not contrary to the national interest.

[2]

- The Australian regime's screening thresholds are set by regulation, meaning no change to the primary legislation was required. Australia already had a national interest test as part of its foreign investment review framework, which also helped to reduce complexity associated with implementing the temporary measures. The national interest test Cabinet agreed to as part of the Phase Two reform of New Zealand's screening regime is based on Australia's test.

[2]

- Ordinarily, Australia applies the following monetary screening thresholds:
 - \$0 for all investors in existing residential properties,
 - \$1.2 billion for FTA partner country private investors in agricultural land,
 - \$50 million for non-FTA partner country private investors in agricultural land,
 - \$1.2 billion for FTA partner country private investors in non-sensitive businesses (except for media, which has a \$0 threshold),
 - \$275 million for FTA partner country private investors in sensitive businesses and for non-FTA partner country private investors in any business, and
 - \$0 for all foreign government investors in any land and any business.

Canada

- Canada's foreign investment review framework already allowed for the review of all proposed foreign investments of any value that may be injurious to national security (i.e. it already has a \$0 monetary screening threshold) by the responsible Minister. There is no statutory definition of 'national security', but the Canadian government publishes a list of factors that may be considered when assessing whether an investment poses a national security risk.
- In mid-April, Canada announced that certain foreign investments would face enhanced scrutiny, regardless of their monetary value:
 - investments in certain Canadian businesses related to public health or the supply of critical goods and services, and
 - investments by state-owned investors or state-connected entities.
- The Canadian government also announced changes to how the national security review process will be conducted. These measures will remain in place "until the economy recovers from the effects of the COVID-19 pandemic". The government issued a Ministerial policy statement to bring these changes into effect; [1]

Germany

- Germany announced it would bring forward the establishment of a fund to take stakes in or buy out German companies.
- The German government recently published a draft regulation to increase foreign investment scrutiny in the health sector which is set to come into force on 13 May. The regulation is based on the EU Commission's guidelines urging member states to protect their critical assets and technology.
- The regulation will (among other things):
 - expand the scope of the existing screening regime, in particular to the health sector, requiring notification of transactions where a foreign investor will acquire a 10 per cent or greater interest in a German company that develops, manufactures, or produces medical goods (including vaccines and PPE) for the treatment of highly infectious diseases,
 - clarify that the identity of the foreign investor can be taken into account when screening a transaction, including any links to a foreign government.
- The new rules are likely to enter into effect as soon as mid-May.
- Additional amendments are expected later in the year, including a change to define the 'critical technology' that will be subject to increased scrutiny.

Spain

- 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.

European Union

- 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.

[35] Analyst, International, [39]
Thomas Parry, Manager, International, [39]