

The Treasury

Reform of the Overseas Investment Act Information Release

May 2020

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Office of the Associate Minister of Finance (Hon David Parker)

Chair,

Cabinet Economic Development Committee

COVID-19 Economic Response: reform of the Overseas Investment Act 2005

Proposal

- 1 This paper seeks agreement to:
 - 1.1 policy decisions on the design of the reform package for the reform of the Overseas Investment Act 2005 (the 'Act') in response to the COVID-19 pandemic,
 - 1.2 procedural decisions to implement the Overseas Investment (COVID-19 Emergency Measures) Amendment Bill and the Overseas Investment (Other Measures) Amendment Bill under a split bill legislative process,
 - 1.3 introduce the attached Overseas Investment (COVID-19 Emergency Measures) Amendment Bill on 14 May 2020,
 - 1.4 deal with the Overseas Investment (COVID-19 Emergency Measures) Amendment Bill ^[33] ,
 - 1.5 introduce the attached Overseas Investment (Other Measures) Amendment Bill, and
 - 1.6 withdraw the Overseas Investment Amendment Bill (No 2).
- 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 The Act provides a framework for regulating foreign investment in sensitive New Zealand assets, being sensitive land, significant business assets and fishing quota. It seeks to balance the government's objective of supporting high quality investment, while ensuring the government has the necessary tools to manage the risks associated with foreign investment.
- 4 The Phase Two reform of the Act (which Cabinet endorsed in November 2019) aimed to improve the balance struck by the Act, through strengthening the government's ability to manage high risk investments with the introduction of a national interest test, and removing consent requirements for a range of low risk transactions, such as minor adjustments to existing shareholdings.

- 5 The COVID-19 global pandemic and related economic downturn have changed the foreign investment risk environment. In particular, they have intensified issues identified in the Phase Two reform of the Act and revealed additional issues, resulting in:
 - 5.1 failing or distressed firms increasing the risk of overseas investors being able to acquire ordinarily productive firms or strategically important assets at 'fire sale prices' without government scrutiny. This may be with an intention of undermining New Zealand's national security, result in a transfer of knowledge and jobs, or the loss of entry points into global value chains or control of cornerstone businesses in sectors displaced by the COVID-19 pandemic. These would all trigger a corollary reduction in long-term domestic living standards, and
 - 5.2 an increasing number of economically distressed firms will require quick access to debt and equity finance to remain viable, and many such transactions currently require consent. Regulatory impediments to the flow of capital can compromise a firm's survival.
- 6 To date, the Government has announced approximately \$20 billion of direct fiscal support measures for businesses, which sit alongside the easing of monetary policy, to cushion the negative economic impacts. These measures provide financial support to firms, reducing their need for foreign investment (and the associated risks around loss of control). However, by themselves, these measures are unlikely to be sufficient to guarantee ongoing business viability. Firms will still need to access external capital, including, in some cases, foreign capital, to remain viable.
- 7 It is critical that the government is able to manage the risks associated with such transactions, but equally, that Crown intervention does not delay investment that protects jobs and economic growth. This kind of foreign investment will be vital to New Zealand's economic resilience during the pandemic, and to our growth in the recovery.
- 8 The reform package in this paper contains measures that respond to the heightened security and economic risks presented by the COVID-19 pandemic, which form part of the attached Overseas Investment (COVID-19 Emergency Measures) Bill ('Emergency Measures Bill'). They build on many of the changes agreed to by Cabinet under the Phase Two reform. These changes augment the Government's business response package, protecting those businesses important to our national security, economy, and communities. In particular, I propose:
 - 8.1 temporarily requiring investors to notify the government of all foreign investment transactions, regardless of the monetary value, that would result in more than 25 per cent foreign ownership of a firm or its assets. If necessary, these transactions can then be assessed for consistency with the national interest (and that the government publish clear guidance on what constitutes the national interest to inform this assessment),
 - 8.2 exempting two classes of low risk but economically important transactions in the financial sector that are necessary to support lending to New Zealand, and

8.3 introducing new regulation making powers to manage transitional risks associated with the rapid development, drafting and implementation of these proposals.

9 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, in comparable ways to what I propose in this paper.

[1]

11 These measures, along with many of the changes agreed to in the Phase Two reform are needed urgently to protect New Zealand's economic, security and other essential interests. I propose implementing these changes via a 'split bill' legislative process under which:

11.1 the urgent Emergency Measures Bill (attached) is introduced and subject to a one week Select Committee process before being passed [33]
This Bill comprises the new tools proposed in this paper as well as the provisions of the Phase Two Reform Bill most critical to the Government's COVID-19 response,

11.2 the non-urgent Overseas Investment (Other Measures) Amendment Bill ('Other Measures Bill') (attached) is introduced concurrently and referred to the Select Committee. This Bill would contain the remaining provisions of the Phase Two Reform Bill.

12 To further ensure the contents of the urgent Emergency Measures Bill are subject to appropriate Parliamentary and public scrutiny, the Select Committee reviewing the Other Measures Bill would also be given scope to consider and recommend changes to the enduring provisions enacted under the urgent Emergency Measures Bill. This would occur after the Emergency Measures Bill has been passed into law.

Relation to government priorities

13 This paper is part of the Government's economic response to COVID-19. The proposals in this paper will help to secure and support the business sector and manage foreign investment risks, supporting New Zealanders' wellbeing.

14 The investment screening tools in this paper need to work in tandem with the range of business support policies that respond to COVID-19. A decision to block foreign investment, which is the most significant tool in this paper and which should be used rarely, needs to be made with regard to the other sources of finances a firm can access, if they are to continue trading. The proposals in this paper have been designed with regard to:

- 14.1 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

[33]

Policy

- 15 The Overseas Investment (COVID-19 Emergency Measures) Amendment Bill ('Emergency Measures Bill') will implement the policies proposed in this paper, and some aspects of the Overseas Investment Amendment Bill (No 2) ('Phase Two Reform Bill'), as agreed by this Committee on 6 May 2020. The Overseas Investment (Other Measures) Amendment Bill ('Other Measures Bill') will implement the remaining aspects of the Phase Two Reform Bill and will be referred to the Finance and Expenditure Committee.
- 16 Changes to the overseas investment screening regime require legislative action because screening is governed by the Overseas Investment Act 2005 ('Act'). The Emergency Measures Bill has an urgent priority.

Background

Regulating foreign investment in New Zealand's sensitive assets

- 17 The Act is New Zealand's principal tool for regulating foreign investment in New Zealand's sensitive assets.¹ The Act provides a framework for screening foreign investments in sensitive land (which includes farmland, the foreshore, and lakebed), significant business assets (generally assets valued at or above \$100 million),² and fishing quota to ensure that they benefit New Zealand.³ It seeks to balance the need to support high quality investment with ensuring the government has the necessary tools to manage the risks associated with foreign investment.

Phase Two reform sought to improve the government's ability to manage high risk investments, remove overreach and simplify consent processes

- 18 This Government is concerned that the Act does not currently strike the right balance. The perceived complexity of the consent framework by overseas investors primarily relates to the consent framework for sensitive land (which I note has not prevented the primary sector achieving success internationally). The threshold tests to acquire significant business assets are low. This is demonstrated by the low level of declined applications to acquire significant

¹ By some measures, 15 per cent of foreign investment into New Zealand is covered by the Act.

² An investment amounts to the acquisition of a sensitive business asset where the value of the consideration or the securities provided for the assets acquired (including property and other intangible assets) exceeds \$100 million. For foreign investors from countries with which New Zealand has entered a free trade agreement (FTA), alternative higher monetary thresholds for investments in significant business assets are prescribed in those FTAs.

³ For the purposes of the Bills, overseas persons are broadly non-New Zealand citizens and residents, bodies corporate, and other unincorporated entities that are more than 25 per cent owned or controlled by overseas persons.

business assets over the past five years. The high concentration of overseas ownership in many industry sectors including banking, insurance, and supermarkets also demonstrates this. The current Act does not give the government tools to adequately manage risks to our national security and other national interests. Conversely, there is unnecessary complexity for some of the transactions caught by the current regime such as minor changes in shareholding, some listed company transactions, some debt instruments, and rules relating to good character.

- 19 The Phase Two reform aimed to achieve a better balance in the Act. In November 2019, Cabinet agreed to comprehensive set of changes [CAB-MIN-0593 refers]. Core elements of the reform include:
- 19.1 the introduction of tools to enhance the government's ability to manage the risks associated with foreign investment:
 - 19.1.1 the national interest test, which will enable the government to decline any investment ordinarily subject to consent that is considered contrary to New Zealand's national interest, and
 - 19.1.2 the national security and public order call-in power, which will allow the government to impose conditions on, block or unwind certain transactions not ordinarily screened under the Act that pose a significant risk to New Zealand's national security or public order, and
 - 19.2 reducing unnecessary red tape by:
 - 19.2.1 streamlining the investor test and benefits test consent pathways,
 - 19.2.2 no longer screening fundamentally New Zealand entities, such as listed companies that are majority owned and controlled by New Zealanders,
 - 19.2.3 no longer screening a range of land simply because it adjoined land that was sensitive in its own right, and
 - 19.2.4 no longer screening minor changes to shareholding that do not materially impact on the ownership or control of sensitive assets.

20 On 19 March 2020, the Phase Two Reform Bill was introduced to the House.

COVID-19 and the foreign investment risk environment

COVID-19 and the economic downturn are increasing foreign investment risks

- 21 The COVID-19 pandemic has disrupted the global economy and triggered a severe economic downturn. Public health measures taken by governments across the world to restrict public transmission, together with the economic disruption, are combining to increase the risks posed by foreign investment, as:

21.1 the value of some ordinarily productive firms are falling below the threshold at which investments can be subject to review.⁴ This risks increasing opportunities for overseas persons to acquire large New Zealand businesses at 'fire sale prices', resulting in ownership and control of economic activity moving outside New Zealand, [1]
and

21.2 an increasing number of distressed firms will require quick access to debt financing to remain viable. Although most lending transactions are low risk, these economically critical transactions typically require consent and are therefore subject to regulatory delays. Delays risk threatening the viability of some firms, and incentivise foreign equity injections above debt financing, despite equity investments posing greater risks.

22 Other comparable jurisdictions have already taken steps to enhance protection of their essential interests in response to the pandemic-related risks, such as Australia, Canada, Spain, Germany and the EU.

23 The national interest test and other changes agreed to in the Phase Two reform will improve the government's ability to manage many of the economic, security and welfare risks revealed and amplified by the pandemic, though they cannot not fully address them. These risks will also persist in the immediate aftermath.

Government economic response will improve liquidity, though firms will have ongoing unmet capital needs

24 The Government's economic response package is on an unprecedented scale. The business support measures aim to improve liquidity in the short to medium term (through wage subsidies and tax-loss carry-back mechanisms), facilitate the supply of credit (through the finance guarantee) and support solvency through the easing of some insolvency requirements. These measures help preserve firm value and therefore reduce the need for additional financing. This contributes to the management of foreign investment risks.

25 Despite the scale and coverage of this package, I expect that some firms will remain in need of urgent access to additional capital (via debt financing or equity injections) to remain viable now, and grow in the post-pandemic recovery phase. In some cases, it may be difficult or inappropriate for the Crown to capitalise firms. For these firms, the best source of that capital will be from private domestic and foreign investment. This increases the need to:

25.1 manage the foreign investment risks associated with those capital flows,
and

25.2 address the distinct features of the Act (not present in comparable regimes) that limit firms' access to low risk capital at this critical time.

⁴ That is, the value of the consideration, securities, or assets is less than the screening threshold set out in the Act or the alternative monetary thresholds prescribed in FTAs. The Act requires consent for most investments of \$100 million or greater. In general terms, this threshold increases to \$200 million for investors covered by the Comprehensive and Progressive Trans-Pacific Partnership, and to \$537 million for Australian non-government investors under the Closer Economic Relations Investment Protocol.

New COVID-19 response tools to manage pandemic-related risks

- 26 This paper puts forward proposals to address these pandemic-related risks, which build on the substance of the Phase Two Reform Bill, by:
- 26.1 improving the government's ability to review transactions not ordinarily screened, and
 - 26.2 removing impediments to low risk lending transactions, helping to secure firm viability during the crisis and support economic growth in the aftermath.
- 27 These proposals have been combined with certain changes from the Phase Two Reform Bill deemed critical to the Government's COVID-19 response, to form the Emergency Measures Bill. The new tools will ensure that the Government is well positioned to support the economy and protect New Zealand's national interest during this period.
- 28 The proposed COVID-19 response tools were assessed against the same criteria used in the Phase Two reform. These broadly consider the extent to which the options:
- 28.1 manage risks associated with foreign investment,
 - 28.2 support investment in productive assets, and
 - 28.3 result in more transparent, predictable or timely outcomes.
- 29 The regulation making powers were also assessed for consistency with legislative best practice.
- 30 All proposals were designed to maximise consistency with equivalent processes, concepts or powers contained in the Act (as amended by the Phase Two Reform Bill) or the Overseas Investment Regulations 2005 ('Regulations'), wherever possible. This is essential to support stakeholder understanding of the changes, and agencies to develop, communicate and implement the changes.
- 31 This paper also seeks agreement to a 'split bill' process for passage of the Emergency Measures Bill and the Other Measures Bill.
- 32 These proposals will not change the treatment of assets that are already screened under the Act, such as investments in farmland.

New power to require notification of investments in businesses not ordinarily subject to review

New emergency notification power to require notification of all investments in existing businesses and business assets.

- 33 To empower the government to better manage threats to the national interest arising because of the economic impact of the pandemic, I propose introducing a temporary emergency notification power. The power would require overseas persons to notify the government of any investment in an existing business or certain business assets that would not ordinarily require consent. The

government would be able to assess the notified transactions to determine whether they are contrary to New Zealand's national interest.⁵ Broadly speaking, this power would:

- 33.1 apply to controlling investments of any value by overseas persons in existing businesses. That is, the acquisition of a more than 25 per cent interest in the business, or the increase in an existing holding to or beyond a 50, 75 or 100 per cent interest, for a transaction of any value,
 - 33.2 apply to investments in business assets of any value that effectively amount to a change in control of the underlying business. This would be defined in regulations as transactions that result in an overseas person acquiring more than 25 per cent of the total value of a New Zealand business' assets (calculated before the acquisition),
 - 33.3 require investors to notify the regulator of transactions within scope,
 - 33.4 empower the responsible Minister to take action in respect of transactions that are contrary to New Zealand's national interest, such as imposing conditions, blocking, or unwinding them,⁶
 - 33.5 permit transactions where no action is taken to proceed quickly, and preclude the government from taking action in respect of those transactions in future,⁷
 - 33.6 impose statutory timeframes on the review of notified transactions,
 - 33.7 be reviewed every 90 days, and
 - 33.8 be removed once the COVID-19 pandemic or its economic aftermath cease to have a significant impact in New Zealand.
- 34 I propose that the emergency notification power operate for an initial period of 90 days from commencement. A periodic review of the power will take place every 90 days [1] [36]

I expect that the power will remain in force for longer than the initial 90 day period, given the wide-reaching impact of the pandemic.

- 35 I propose that the Minister of Foreign Affairs, Minister of Finance and I be delegated authority:
- 35.1 to determine the process and criteria for review of the emergency notification power, and

⁵ This would not apply to transactions exempted from the Act's general consent requirements, including those exemptions agreed to as part of the Phase Two reform, such as investments by qualifying retirement schemes.

⁶ The Minister could impose conditions on the transaction to ensure it is consistent with the national interest. For example, a condition requiring jobs to be maintained in a certain region of New Zealand.

⁷ With the exception of transactions entered into fraudulently or involving misrepresentation.

35.2 to review the power every 90 days to determine whether those criteria continue to be met.

36 This tool will impose a burden on a range of lower-risk transactions, which may impede the flow of beneficial finance and may lead to delays in the processing time for critical transactions.⁸ I considered whether this risk could be addressed by excluding investments in companies with low annual revenue from scope. I decided not to progress this option as it is a blunt mechanism, and would restrict the government's ability to manage important risks (for example, an emerging but high potential start up).

37 Instead, to manage these risks, I propose that Cabinet agrees to:

37.1 a number of 'risk factors' that will allow the regulator and relevant decision maker to rapidly determine whether a transaction could be contrary to New Zealand's national interest [1] , and

37.2 issue public guidance on what matters will always be considered as part of any national interest test assessment, to improve investor certainty and support the regulator and other agencies in undertaking these assessments (see Appendix 2).

38 I propose that the Minister of Finance and I would be able to amend both of these pieces of guidance when necessary over time. For example, this may be necessary to respond to changes in the risk environment, the types of transactions notified under the emergency power, and changes in our broader economic response to COVID-19 to ensure that our approach to supporting the economy remains consistent over time.

39 Finally, to ensure that we can rapidly respond to any future crises that raise similar foreign investment risks, I propose that the government have the ability to introduce a power similar to the proposed emergency notification power through regulations. This would be subject to [1] [36] the Minister of Finance and Minister of Foreign Affairs agreeing that such regulations are an appropriate and proportionate response to the relevant crisis.

Decision making framework for the emergency notification power

40 It is important to be clear about how the emergency notification power will work alongside the existing protections in the Act. Through the Phase Two reform, Cabinet agreed to introduce a national interest test to protect New Zealand's national interest. Under the national interest test, a decision maker can consider the potential risks of a transaction to New Zealand's national interest when deciding whether to grant consent. It will always be applied to transactions that warrant greater scrutiny. If a transaction is determined to be contrary to the national interest, conditions can be imposed to mitigate any risks or consent may be declined. The national interest test is a backstop tool, to be used rarely, and only where necessary to protect New Zealand's national interest.

⁸ Operational risks and the proposed triaging mechanism are discussed at paragraph 75.

- 41 In considering the application of an emergency notification power, and its interaction with the national interest test, the Government must balance two considerations:
- 41.1 The COVID-19 pandemic means that foreign investment will pose greater risks across a wider range of transactions. This justifies the introduction of the emergency notification tool.
 - 41.2 Overuse of the national interest test during the pandemic, or at any time in the future, would risk being seen as protectionist and could reduce New Zealand's attractiveness to foreign investment. This would undermine one of the key priorities of the Phase Two reform.
- 42 As such, the emergency notification power should not:
- 42.1 lower the threshold for exercising the national interest test, or
 - 42.2 result in the inconsistent use of the test across the Act. That is, the national interest test should be applied in the same way, irrespective of whether a transaction is escalated through the emergency notification power or the Act's general consent pathways.
- 43 To reflect these considerations, I propose the following decision making framework to support the emergency power's operation:
- 43.1 the initial decision about whether a notified transaction should be subject to a detailed review against the national interest (in practice, the triaging decision), will rest with me in my capacity as Associate Minister of Finance, with the potential for this to be delegated to the regulator in the future, and
 - 43.2 any subsequent decision on whether a transaction is contrary to the national interest and should be subject to conditions or blocked will rest with the Minister of Finance (as the Minister responsible for the Act). This power will not be able to be delegated to the regulator.⁹
- 44 I note that assigning the responsibilities in paragraph 43 would need to be achieved through delegation and cannot be achieved through the Act. They would also require a change to existing delegations, given that the Minister of Finance is currently responsible for assessing transactions ordinarily subject to screening under the Act.
- 45 Ministers and the regulator should have the same powers available to support the review of such transactions as if they were transactions ordinarily screened under the Act (as amended by the Phase Two Reform Bill).
- 46 For consistency with the Act, and to support investor and public confidence in the regime, decisions under the national interest test will be made public, except where there exists grounds for withholding under the Official Information Act.¹⁰

9 This is consistent with this Minister's responsibility for making determinations under the national interest test about transactions under the Act generally.

10 For example, where disclosure would raise national security concerns.

Timeframes for decision making under the emergency notification power

- 47 I propose that decision making under the emergency notification power be subject to a statutory timeframe of 40 working days (comprising 10 days for initial triage, after which a large majority of transactions would be able to proceed, and then 30 days for national interest assessment if it is required), plus a 30 day extension period.
- 48 The overall timeframe will be set in the Regulations, and I intend to publicly signal that triage will occur within 10 working days. Consistent with the Phase Two reform, a breach of the timeframe will not affect the validity of the decision or give rise to any legal liability.
- 49 These timeframes aim to quickly filter out transactions where there are few risks, and allow time to focus on significant transactions. The timeframes will be challenging for the regulator, agencies and Ministers to achieve.

Trade-offs associated with the exercise of the national interest test

- 50 The proposed design of the emergency notification power balances the need to manage foreign investment risks, while ensuring a majority of transactions can be processed quickly without requiring government action.
- 51 In some rare cases, exercising the national interest test may result in a transaction being blocked. This could result in a firm needing to close, unless another source of capital can be found. The Minister will need to consider the potential for this outcome when exercising any such power.
- 52 While this may result in requests for Crown funding, I consider that the threshold for imposing conditions on, or blocking, a foreign investment transaction is lower than the threshold for Crown funding, given the additional costs and risks that Crown funding places on taxpayers. In practice, this may mean that a proposed transaction could be blocked with the effect that the business fails, even where the Crown is unlikely to take an equity interest to keep it operating.
- 53 I propose that Cabinet authorise the Minister of Finance and I to take second order design decisions to refine the proposed risk factors for triaging applications and the national interest test considerations. This may be necessary, for example, to respond to the types of transactions and notifications received under the emergency notification tool and changes in our broader economic response to COVID-19 to ensure that our approach to supporting the economy remains consistent over time.

Exemptions for low risk transactions that provide capital flows to firms

- 54 Cabinet endorsed changes to existing exemptions for low risk transactions that enable firms to raise equity as part of the Phase Two reform.¹¹ The pandemic has intensified the need for timely introduction of those exemptions, but has also

11 Cabinet agreed to make amendments to allow an unlimited number of restructures of a corporate by an overseas entity where there is no change in the ultimate ownership or control of the company, and to allow minor adjustments to existing shareholdings that do not cross control thresholds (T2019/3412 and DEV-19-MIN-0825 refer).

highlighted long-standing issues with consent requirements that limit the ability of banks to lend and manage risk across the economy,¹² including that:

54.1 many of New Zealand's largest financial institutions require consent to issue large scale loans valued at over \$100 million, despite the bank only acquiring a claim over cash flows and not the real asset,¹³ and

54.2 overseas persons acquiring securitised loan parcels valued at more than \$100 million from lenders require consent to do so, again despite the transaction only granting the overseas person a right to cash flows associated with the underlying loans.¹⁴

55 I propose making minor expansions to two longstanding exemptions to remove these classes of lending and loan portfolio management transactions. In particular, these proposals would remove consent requirements for:

55.1 the issuance of loans by registered banks, and

55.2 the acquisition of parcels of securitised loans by overseas persons.

56 The proposed new exemptions are very low risk, as the transactions do not confer an interest in the underlying sensitive asset (the firm or its assets), instead only granting an interest in revenue flows generated by the firm. However, to protect the integrity of the Act, I propose that any residual risks be managed by imposing statutory constraints on both exemptions in line with those successfully applied to other exemptions.¹⁵ Limiting the lending exemption to registered banks regulated by the Reserve Bank of New Zealand (RBNZ) adds a further layer of protection.

57 I note that these exemptions would be implemented as standing consents under the Emergency Measures Bill, rather than through an amendment to the Regulations. These standing consents will be transitional only, and will be replaced in the Other Measures Bill by permanent carve outs and exemptions as agreed by this Committee.

58 The proposed emergency notification power will intensify the need to remove the regulatory barrier to lending and portfolio management transactions. This is because without change, these kinds of lending transactions would require notification, increasing the regulatory triage/assessment burden caused by the emergency notification power.

59 These exemptions encourage lending to the real economy, preventing the unnecessary offshore transfer of wealth and knowledge. I expect these

12 Regulations 41 and 42, Overseas Investment Regulations 2005.

13 This is because the loan is treated as a significant business asset in its own right, requiring consent under the Act.

14 Transactions to acquire securitised assets that grant an interest in sensitive land and fishing quota do not require consent, by contrast.

15 This includes that the transaction is entered into in the ordinary course of business, that both parties are acting in good faith, and that the transaction is not entered into with the intent of acquiring the sensitive assets that underlie the relevant loans (the business assets or similar that may secure the loans).

amendments will have a positive impact on welfare and domestic living standards.

New regulation making powers

The complexity and speed involved in developing these proposals risks unintended capture, transitional issues and potential errors

60 The proposals in the Emergency Measures Bill are complex, will considerably expand the Act's coverage, have necessarily been developed quickly and will be passed without ordinary Parliamentary scrutiny. As such, the Bill could result in:

60.1 unintended capture of a broad range of economically important but low risk transactions that warrant less stringent review, or no review at all. Screening such transactions could restrict economic growth, and

60.2 policy design and legislative drafting that has significant unforeseen transitional issues or errors, which may undermine the credibility of the broader reforms and prevent the processing of transactions essential to firm viability.

61 To help resolve these issues, I propose introducing two regulation making powers that collectively:

61.1 Regulation making power one: a power that enables the Minister¹⁶ to:

61.1.1 recommend the exemption of any transaction, person, interest, right, asset, or classes of the aforementioned from consent requirements, for the purpose of responding to an epidemic in New Zealand, and

61.1.2 enables the Minister to recommend amendments to consent requirements for most classes of transactions, where necessary to respond to an epidemic in New Zealand.

61.2 Regulation making power two: enables the Minister, in limited circumstances, to recommend the modification of provisions of the Act, where necessary or desirable for the orderly implementation of the Act and consistent with the intended purpose of the relevant provisions.

62 Recognising that the need for these powers is temporary, I propose that these powers be repealed by the enactment of the Other Measures Bill.

One power gives rise to rule of law issues but is justified in these circumstances

63 The second regulation making power would enable the Act (primary legislation) to be amended through Regulations. [36]

16 The relevant Minister would be the Minister responsible for the Act, unless responsibility for regulation making has been delegated. For example, I (in my capacity as Associate Minister of Finance) currently have delegated authority to recommend that exemptions be made.

- 64 This type of power has previously been used to manage transitional issues associated with the introduction of complex legislation.¹⁷ Given the scope and complexity of this legislation, and the potentially significant economic costs associated with any transitional issues or unforeseen or unintended consequences, I consider it is appropriate to introduce this power in the current circumstances.
- 65 In addition to this regulation making power being time-limited, I propose to preserve fundamental rule of law protections by limiting its application to addressing errors or ambiguities introduced through the Emergency Measures Bill (and preclude its use to resolve any other issues with the Act). The power will include a requirement that the Minister be satisfied that the regulations are necessary or desirable for the orderly implementation of the Act, and consistent with the intended purpose of the relevant provisions.

Process

A 'split Bill' legislative process allows for urgent enactment of COVID-19 response tools, while providing for scrutiny of Phase Two reforms

- 66 An immediate response that resolves the new and longstanding issues with the Act is needed to ensure the Act can be used to manage the escalating security and economic risks caused by the COVID-19 pandemic and protect domestic living standards.
- 67 Despite the urgency of the current circumstances, it is important that any changes to the Act are subject to Parliamentary and public scrutiny. The condensed timeframes for the design and drafting of the COVID-19 response tools increase the need for a credible review of the reform package.
- 68 To balance these competing priorities, I propose to progress the Phase Two reforms and the changes proposed in this paper through two separate Bills (a 'split bill' process). That is:
- 68.1 the urgent Emergency Measures Bill is introduced ^[33], including being subject to a one week Select Committee process. This Bill comprises the additional reforms proposed in this paper as well as the provisions of the Phase Two Reform Bill most critical to the Government's COVID-19 response,
- 68.2 the non-urgent Other Measures Bill is introduced, referred to Select Committee and progressed on an ordinary legislative track. This Bill would contain the remaining provisions of the Phase Two Reform Bill (that is, those not critical to the COVID-19 response) and
- 68.3 the original Phase Two Reform Bill would be withdrawn.
- 69 To further ensure the contents of the urgent Emergency Measures Bill are subject to appropriate Parliamentary and public scrutiny, the Select Committee reviewing the Other Measures Bill would also be given scope to consider and recommend

17 For example, the enactment of the Financial Markets Conduct Act 2013. Refer to section 547 of that Act.

changes to enduring provisions enacted under the urgent Emergency Measures Bill. This would occur after the Emergency Measures Bill has been passed into law.

- 70 I consider the split bill process is the best way to ensure the Government can protect New Zealand's essential interests against pandemic-related foreign investment risks. It delivers on the Government's objectives for the economic response, while maintaining a channel for the scrutiny of the substance of the Phase Two Reform Bill. I consider there is little drawback to delaying the commencement of the 'non-urgent' features of the Phase Two Reform Bill because some key parts of the reform that would be progressed through the non-urgent Other Measures Bill are already being achieved through alternative mechanisms.¹⁸
- 71 Additional detail about which parts of the Phase Two Reform Bill officials have assessed as being urgent and non-urgent is contained at Appendix 3.

Implementation of certain liberalising measures in Emergency Measures Bill as transitional standing consents

- 72 I recommend implementing certain liberalising measures in the Emergency Measures Bill and Regulations as standing consents.¹⁹ These transactions will remain in scope of the Act, but would be subject to no or reduced screening requirements on a transitional basis. The Other Measures Bill will, if passed, permanently exempt all of these transactions consistent with policy decisions in the Phase Two reform and the decisions made by this Committee. This reflects my view that changes to remove transactions from the Act should not occur without adequate Parliamentary and public scrutiny.

Operationalising the reforms

Transitional risk that new powers cannot be operationalised as quickly as desirable

- 73 The introduction of the emergency notification power will significantly expand the scope of the Act and risks:
- 73.1 creating significant uncertainty, higher workloads and costs for investors, their advisors, and the Overseas Investment Office (OIO, the regulator), and
 - 73.2 slowing low risk, economically valuable transactions that support firm viability.
- 74 To mitigate against these risks, it will be necessary:

18 For example, the higher threshold for investments in farmland is set out in the Government's Ministerial Directive Letter.

19 This applies to the new proposal and agreed changes to remove from consent requirements the following classes of transactions: the issuance of loans by registered banks, the acquisition of securitised loans, transactions by fundamentally-New Zealand entities and managed investment schemes, incremental investments, and some categories of sensitive adjoining land.

- 74.1 for the OIO, together with relevant agencies, to quickly develop new forms, guidance, information sharing, cross-agency governance systems and likely increase resourcing,
- 74.2 to proactively engage with the investment community about the new aspects of the regime,
- 74.3 exercise the use of new regulation making powers to exempt, and streamline consent, for low risk transactions judiciously, and
- 74.4 as outlined above, to provide clear guidance on the types of factors that indicate that a transaction could be contrary to the national interest, as well as the factors that we would always consider when undertaking a full national interest test assessment.

Factors that indicate that a transaction could be contrary to New Zealand's national interest

- 75 I recommend that Cabinet endorse a non-exhaustive set of 'risk factors' to support the rapid determination of whether a transaction could pose risks to New Zealand's national interest. Agencies will develop additional processes and documentation to support triaging consistent with these risk factors. The purpose of the factors is to inform whether national interest concerns may be present in a transaction. They would not be 'bright line' criteria nor a substitute for the in-depth analysis required to determine whether a transaction is contrary to New Zealand's national interest.

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Matters always considered under a national interest assessment

- 79 The emergency notification power will be used where necessary to protect New Zealand's essential interests. The national interest is not defined in the Act but would be determined on a case-by-case basis; this flexibility ensures that the government can respond to changes in the risk environment.
- 80 I propose that Cabinet agree to the publication of guidance specifying a number of matters that will always be considered as part of any national interest test assessment. This would offer additional certainty to investors, advisors and agencies on the operation of the test. The matters that will always be considered when making a national interest assessment include:
- 80.1 whether the investment poses risks to national security, public order and international relations (the security and intelligence agencies are responsible for providing advice on national security matters),
 - 80.2 whether the investment results in the acquisition of a natural monopoly or other business with significant market share,
 - 80.3 the investment's likely economic and social impact,
 - 80.4 the investment's alignment with New Zealand's values and interests and broader policy settings, and
 - 80.5 the character of the investor, including whether it is a foreign government investor.
- 81 While the COVID-19 pandemic and its economic aftermath continue to have a significant impact in New Zealand, I propose that the Government also consider whether the target business is in financial distress. This reflects the increased risk in the current environment that ordinarily productive businesses that make

valuable contributions to New Zealanders' wellbeing could be sold to foreign investors at depressed prices.

- 82 As the foreign investment risk environment changes and our economic response to the COVID-19 pandemic develops, there may be a need to refine the national interest considerations. I recommend that Cabinet authorise the Minister of Finance and I to refine the national interest considerations.
- 83 The proposed guidance is provided at Appendix 2.

Managing transactions during an election period

- 84 There will be urgent decisions under the Act (both applications for consent and notifications under the new emergency power) that will need to continue to be taken during 2020 General Election period.
- 85 In the period leading up to the general election, there is no formal constraint on Ministers continuing to make decisions under the Act.
- 86 Following the election and before a government is formed, in accordance with the caretaker convention, Ministers (or the regulator on delegation) can continue to make decisions under the Act, but significant decisions (for example, decisions to block a transaction on national interest grounds) should be made in consultation with other political parties or on the advice of the incoming government (as relevant).

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Legislative Implications

- 98 The new proposals in the Emergency Measures Bill will require changes to the Act and the Regulations. This Bill is to be introduced to the House under urgency on 14 May 2020.
- 99 Proposals in the non-urgent Other Measures Bill will modify the Act and the Regulations. It is proposed this Bill also be introduced on 14 May 2020, complete its first reading shortly after that and then be referred to Select Committee.
- 100 The Phase Two Reform Bill was assigned priority four on the 2019 Legislative Programme and was introduced to the House on 19 March 2020. This Bill will be withdrawn from the House ahead of the introduction of the Emergency Measures Bill and Other Measures Bill.

Impact Analysis

Regulatory Impact Statement

- 101 The Treasury has determined that this proposal is a direct Covid-19 response and has suspended the Regulatory Impact Assessment requirements in accordance with the Cabinet decision [CAB-20-MIN-0138 refers]. The Treasury has included all available analysis in this paper.
- 102 A Regulatory Impact Assessment (RIA) was prepared in accordance with the necessary requirements and was submitted at the time approval was sought for the policy relating to Phase Two Reform Bill [CAB-19-MIN-0593 refers]. The RIA was updated to reflect policy decisions I made under authorisation from DEV.

Population Implications

- 103 There are no population group impacts arising from these proposals.

Human Rights

- 104 There will be human rights implications arising from this paper.

Freedom from discrimination

- 105 The Act and the proposed emergency notification power treats New Zealanders and foreign nationals differently, and so discriminates on the basis of national origin, which engages the right to freedom from discrimination (on the grounds of national origin) under the New Zealand Bill of Rights Act 1990 (the 'BORA').²⁶

[33]

26 The emergency notification power does not distinguish between foreign nationals.

- 106 I consider that this limit on freedom from discrimination is justifiable. The objective of the proposed reform is to ensure the government can protect New Zealand's essential economic and security interests from the risks associated with foreign investment caused by the COVID-19 pandemic and economic downturn. They ensure that the government can prevent or manage an investment where the risk to New Zealand's national interest outweighs any potential benefit. This objective is sufficiently important to justify a limitation on the right to be free from discrimination.
- 107 The proposed changes do not limit the right more than reasonably necessary. In particular:
- 107.1 nationality is not the exclusive determinant of whether a person will be treated as an overseas person under the Act,
- 107.2 the emergency notification power will only be used to manage risks to New Zealand's essential security and other national interests,
- 107.3 some of the proposals eliminate screening altogether where it is not warranted by the risk profile of the transaction.

Compliance

- 108 In the available time officials have not been able to make a full assessment of all the compliance risks. On the basis that the Emergency Measures Bill and Other Measures Bill do not materially differ in intention from the Phase Two Reform Bill recently approved by Cabinet, I consider they comply with:
- 108.1 the principles of the Treaty of Waitangi,
- 108.2 the rights and freedoms contained in the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993 (this is provisional on BORA vetting),
- 108.3 the disclosure statement requirements,
- 108.4 the principles and guidelines set out in the Privacy Act 1993, and
- 108.5 the *Legislation Guidelines* (2018 edition), maintained by the Legislation Design and Advisory Committee.

Consultation

- 109 This paper was developed in consultation with the Department of Prime Minister and Cabinet, Ministry of Foreign Affairs and Trade (MFAT), Ministry for Culture and Heritage, Ministry of Primary Industries, the New Zealand Security Intelligence Service, the Government Communications Security Bureau, Ministry of Business, Innovation and Employment, New Zealand Trade and Enterprise, Land Information New Zealand and the OIO.
- 110 An exposure draft of the Emergency Measures Bill will not be released due to time limitations. However, officials have consulted on parts of the draft legislation with a small group of technical experts to ensure that the Bill will operate as intended and to begin to build understanding of the reforms within the industry.

Further, the Phase Two Reform Bill, which contains all the previously agreed Phase Two reform changes, has been publicly available since it was introduced to the House on 19 March 2020.

- 111 This Bill will continue to meet the commitment in the Coalition Agreement between the New Zealand Labour Party and New Zealand First to “strengthen the Overseas Investment Act”.
- 112 Consultation with the government caucus and other political parties has been undertaken.

Binding on the Crown

- 113 The principal Act binds the Crown and the Emergency Measures Bill and Other Measures Bill will be binding upon the Crown on commencement.

Allocation of decision making powers

- 114 The Emergency Measures Bill introduces new decision making powers and procedures, which have been drafted consistently with the criteria relating to the qualifications and responsibilities of decision makers.
- 115 The new emergency notification power will be used to screen investments that may be contrary to New Zealand’s national interest which are not ordinarily screened under the Act. It will include powers to unwind, prohibit and place conditions on transactions. I have proposed that the Minister responsible for the Act be responsible for exercising the national interest test in all circumstances. This reflects the high threshold in the national interest test and the principle that decisions made under that test should be consistent across the Act.

Associated regulations

- 116 A combination of new regulations, existing regulations and amended regulation making powers will be required to give full effect to the policy that the Emergency Measures Bill is intended to implement.
- 117 The Bill allows timeframes to be set in regulations for all decisions to provide greater certainty to investors. The Regulations will set a timeframe for decision under the new emergency power
- 118 New regulations will be needed to bring some of the new COVID-19 response tools into effect. This includes thresholds for determining what assets should be subject to screening.
- 119 The exemption criteria in the Act will be amended to enable relevant changes to consent requirements as proposed in this paper and agreed in the Phase Two reform, including for the two additional classes of low risk lending transactions.

Other instruments

- 120 The Emergency Measures Bill does not include any provision empowering the making of other instruments that are deemed to be legislative instruments or disallowable instruments.

Definition of Minister/department

- 121 No changes to the current definition of Minister are proposed. The principal Act does not contain a definition of a department.

Commencement of legislation

- 122 The urgent Emergency Measures Bill will come into force in the following two stages:²⁷
- 122.1 the investor test and the changes to clarify consideration of negative impacts in the benefits test would commence by Order in Council, and
- 122.2 the remainder of the Bill will come into force two weeks from the date of Royal Assent.
- 123 The new measures would apply to transactions entered into after those dates. The existing principal Act rules will continue to apply to all transactions entered into before the commencement date, including 'conditional agreements' for sale and purchase where conditions precedent are not met yet and the contract is not yet enforceable at the commencement date.
- 124 The non-urgent Other Measures Bill will be enacted within 12 months of introduction, unless provisions are brought into force earlier by Order in Council.
- 125 If necessary, the commencement method or date may be amended during the Bill's passage through the House.

Parliamentary stages

- 126 The urgent Emergency Measures Bill should be introduced and complete its first reading under urgency on 14 May 2020, then be referred to the Finance and Expenditure Select Committee for a one week review process for report back by 18 May 2020. [33]
- 127 The non-urgent Other Measures Bill, which will implement the remaining changes agreed to under Phase Two, should also be introduced on 14 May 2020, and complete its first reading before being referred the Finance and Expenditure Committee. As part of the Committee's review process, the Committee will also have scope to consider, and provide recommendations on, enduring provisions passed in the Emergency Measures Bill (this would be after that Bill has been passed).
- 128 The Phase Two Reform Bill was introduced on 19 March 2020. This Bill will be withdrawn from the House prior to the introduction of the urgent and non-urgent Bills discussed above.

27 Refer Appendix 3 for additional detail about the timings of commencement of different parts of the Emergency Measures Bill.

Communications

- 129 I plan to publicly announce the policy decisions in this paper shortly after Cabinet has made decisions.
- 130 The Emergency Measures Bill would temporarily tighten the screening regime. I expect this reform will attract comment from a range of stakeholders with divergent perspectives on this temporary strengthening, as well on the [33]

In particular, I expect that:

- 130.1 investors, their advisors and the business community may have concerns about the coverage of the temporary emergency notification power,
- 130.2 many small and medium businesses that do not ordinarily interact with the Act or the regulator may find it difficult to understand the nature of the changes and the implications for their business,
- 130.3 the public, including individuals and civil society groups, may oppose the process for passing the Emergency Measures Bill under urgency without opportunity for comment, and
- 130.4 many of New Zealand's international partners (including those who have previously been closely engaged with the Phase Two reform) will closely monitor the consistency of the proposals with New Zealand's international legal and trade obligations.
- 131 It will therefore be important for the Government to continue to publicly articulate:
- 131.1 the value of foreign investment, particularly where it supports low risk capital flows and that New Zealand remains open to productive, high-quality foreign investment,
- 131.2 the need for an effective screening regime to protect New Zealand's national security, public order, and economic and welfare interests,
- 131.3 the changes respond to the COVID-19 pandemic, are time-limited,²⁸ and consistent with our international obligations, and
- 131.4 that there will be opportunity for Parliamentary and public scrutiny of the entirety of the Phase Two reform package under this legislative process.
- 132 This messaging will be critical to generate public understanding and support for these proposals. Officials have prepared a communications package for the public announcement of these reforms, which includes:

28 The regulation making powers in the Emergency Measures Bill will be repealed by the enactment of the Other Measures Bill. The emergency notification power will be periodically reviewed and deactivated when the criteria for its imposition are no longer met.

- 132.1 material to support investor/advisor and business understanding of the changes, and
- 132.2 material to support engagement with New Zealand's international partners, which has been prepared together with MFAT. [1]

[36]

Proactive Release

134 I intend to publish this Cabinet paper when this reform is announced, subject to redactions as appropriate under the Official Information Act 1982.

[1] [36]

Recommendations

I recommend the Committee:

New COVID-19 response tools to manage pandemic-related risks

- 1 **Note** that the proposals in this paper support the Government's economic response to COVID-19 by helping to secure and support the business sector and manage foreign investment risks.
- 2 **Note** that the investment screening tools in this paper are designed to work in tandem with the range of business support policies that respond to COVID-19, and that I will continue to ensure they are complementary, as our economic response package develops further.

New power to require notification of investments in business ordinarily not subject to review

- 3 **Note** that the pandemic and related economic downturn will increase the risk that some overseas investment undermines New Zealand's national security, or

results in the transfer of ownership and control of economic activity for prices that do not reflect their true value to New Zealand.

- 4 **Note** that the Overseas Investment Act 2005 (the Act) does not enable the government to manage the risks to New Zealand's essential interests posed by such investments where they fall below its monetary screening threshold.

Emergency notification power for all investments in existing businesses and certain business assets not ordinarily requiring consent

- 5 **Agree** to introduce a temporary emergency notification power that would require an overseas person to notify the government of any investment in an existing business or certain business assets that would not ordinarily require consent.
- 6 **Agree** that the temporary emergency notification power would:
 - 6.1 apply to controlling investments of any value by overseas persons in existing businesses. That is, the acquisition of a more than 25 per cent interest in the business, or the increase in an existing holding to or beyond a 50, 75 or 100 per cent interest,
 - 6.2 apply to investments in business assets of any value that effectively amount to a change in control of the underlying business. This would be defined in regulations as “transactions that result in an overseas person acquiring more than 25 per cent of the total value of a New Zealand business’ assets (calculated before the acquisition)”,
 - 6.3 require investors to notify the regulator of transactions within scope,
 - 6.4 impose statutory timeframes on the review of notified transactions (according to recommendation 8, below),
 - 6.5 be reviewed every 90 days, and only remain in force while the COVID-19 pandemic, or its economic aftermath, continues to have a significant impact in New Zealand.
- 7 **Agree** that the responsible Minister can impose conditions on, decline or unwind transactions reviewable under the emergency notification power where they are contrary to New Zealand’s national interest.
- 8 **Agree** that the Minister for Foreign Affairs, the Minister of Finance and the Associate Minister of Finance (Hon Parker) be delegated authority:
 - 8.1 to determine the process and criteria for review of the emergency notification power (including its lifetime and withdrawal), and
 - 8.2 to review the emergency notification power every 90 days to determine whether those criteria continue to be met.
- 9 **Note** that allocating decision making authority in this way could not be achieved through the Act and would require a delegation.

- 10 **Agree** that a similar emergency notification power may be re-established through the Regulations in future, where necessary to respond to a pandemic or other crisis.

Decision making framework for the emergency notification power

- 11 **Agree** to the following decision making framework for the emergency notification power:
- 11.1 the triage decision about whether a notified transaction could be contrary to the national interest initially rest with the Associate Minister of Finance (Hon Parker) initially, and be able to be delegated to the regulator in future, and
 - 11.2 the determination under the national interest test about whether a transaction is contrary to the national interest, and whether to impose conditions or block the investment, be with the Minister of Finance (as the Minister responsible for the Act and for the national test more generally), and be unable to be delegated to the regulator.
- 12 **Note** that to allocate decision making responsibilities in this way would require delegation and could not be achieved using the Act.
- 13 **Note** that national interest test would remain a backstop tool to be used rarely and only where essential to protect New Zealand's national interest.
- 14 **Agree** that Ministers and regulator have the same powers available to support the review of transactions as if they were transactions ordinarily screened under the Act.
- 15 **Note** that in accordance with previous Cabinet decisions, all decisions on transactions notified under the emergency notification power would be published, except where exists grounds for withholding under the Official Information Act 1982.

Timeframes for decision making under the emergency notification power

- 16 **Agree** that decision-making under the emergency notification power be subject to a statutory timeframe of 40 working days (comprising 10 days for initial triage, and 30 days for national interest assessment), plus a 30 day extension period.
- 17 **Note** that the overall timeframe will be set in the Regulations, and that I intend to publicly commit that the initial triage of notified transactions will occur within 10 working days.

Risks associated with the national interest test

- 18 **Authorise** the Associate Minister of Finance (Hon Parker) and the Minister of Finance to amend the following, where necessary to respond to changes in foreign investment risks or Government priorities:
- 18.1 the proposed risk factors for triaging notified transactions, and

18.2 the national interest test considerations.

Exemptions for low risk transactions that provide capital flows to firms

- 19 **Note** that the pandemic has intensified the need for the timely introduction of two exemptions for transactions that enable firms to raise equity, which were agreed to in the Phase Two reform.
- 20 **Note** that the pandemic has revealed issues with longstanding exemptions that limit banks from lending to the economy and managing their own risk portfolios.
- 21 **Note** that the introduction of the emergency notification power would magnify the regulatory burden associated with such transactions, as they would require notification, triage and review in the absence of an exemption.
- 22 **Agree** to augment the government's business support package to better secure firms and address their capital needs, by extending existing exemptions to remove two additional classes of low risk lending and loan portfolio management transactions from the Act's consent requirements, where:
- 22.1 the transaction is the issuance of a loan by a registered bank, and
 - 22.2 the transaction is the purchase by an overseas person of a parcel of securitised loans.
- 23 **Agree** to limit the exemptions in recommendation 22 to prevent them from being used to circumvent the Act, by requiring that the transaction:
- 23.1 must be entered into in the ordinary course of business,
 - 23.2 occur in good faith, and
 - 23.3 cannot be entered into with the intent of acquiring the sensitive New Zealand assets that underlie the relevant loan.
- 24 **Note** that these exemptions will be implemented as transitional standing consents under the Emergency Measures Bill.
- 25 **Note** that if passed, the Other Measures Bill will permanently exempt these classes of transactions.

New regulation making powers

Transitional issues

- 26 **Note** that these proposals are likely to result in the capture of many transactions that have little to no associated risk.
- 27 **Note** that the rapid development and enactment of the Overseas Investment (COVID-19 Emergency Measures) Amendment Bill ('Emergency Measures Bill') means it may result in unintended transitional issues and errors.

Introduce regulation-making powers to rectify transitional issues

- 28 **Agree** to introduce two new regulation-making powers that can be used to rectify over-capture, transitional issues, and potential errors. These would:
- 28.1 allow for the exemption of individual transactions, persons, interests, rights or assets, or classes of the aforementioned, from consent requirements for the purposes of responding to a pandemic in New Zealand,
 - 28.2 enable the modification of consent requirements for most classes of transactions where necessary to respond to a pandemic in New Zealand, and
 - 28.3 permit the modification of provisions in the Act that have been introduced through the Emergency Measures Bill where necessary or desirable for the orderly implementation of the Act and consistent with the intended purpose of the relevant provisions.
- 29 **Agree** that the power in recommendation 28.3 would be tightly constrained by ordinary public law constraints to ensure any regulation made under this power was consistent with Parliament's intent and no broader than reasonably necessary to rectify the transitional issue.
- 30 **Agree** that the new regulation making powers in the Emergency Measures Bill (recommendation 28, above) would be repealed by the enactment of the non-urgent Overseas Investment (Other Measures) Amendment Bill ('Other Measures Bill').

Process

A 'split Bill' process allows for urgent enactment of critical COVID-19 tools and scrutiny of Phase Two reforms

- 31 **Note** that the Act requires urgent reform to allow the government to manage the escalating economic and security risks associated with foreign investment posed by the COVID-19 pandemic.
- 32 **Note** that the condensed timeframes for design and drafting of the Emergency Measures Bill increase the importance of a credible review of the reform package.
- 33 **Agree** to provide the government with the tools it needs to protect New Zealand's essential interests in the current environment, while maintaining an avenue for proper scrutiny of the Phase Two reforms by:
- 33.1 introducing [33] the Emergency Measures Bill (comprising the proposed new response tools and the provisions of the Phase Two Reform Bill critical to the Government's COVID-19 response, see Appendix 4), including subjecting it to a one week Select Committee process, and

- 33.2 introducing the non-urgent Other Measures Bill (containing the provisions not critical to the COVID-19 response) and referring it to the Finance and Expenditure Select Committee (see Appendix 5),
- 33.3 withdrawing the original Phase Two Reform Bill, and
- 33.4 giving the Finance and Expenditure Select Committee remit to consider and recommend changes to enduring provisions enacted under the urgent Emergency Measures Bill after it has been passed into law, when that Select Committee reports back to Parliament on the Other Measures Bill.

Operationalising the reforms

Factors that indicate a transaction could be contrary to New Zealand's national interest

- 34 **Note** that change to require notification of foreign investments will result in an increased volume of transactions for the regulator to triage and process, and may capture low risk transactions that provide critical capital to firms.
- 35 **Note** that effective triaging is critical to manage these consequences.

[1] [33]

- 37 **Authorise** the Minister of Finance and the Associate Minister of Finance (Hon Parker) to refine the list of risk factors, where necessary over time.

Implementation of certain liberalising measures in Emergency Measures Bill as transitional standing consents

- 38 **Agree** to implement the proposed new exemptions for low risk lending transactions and certain agreed liberalising measures from the Phase Two reform as transitional standing consents under the Emergency Measures Bill.
- 39 **Note** that if passed, the Other Measures Bill will permanently exempt all of these transactions.

Matters always considered under a national interest assessment

- 40 **Note** that the introduction of the national interest test will create considerable uncertainty for investors and the regulator, which together with concern about processing delays, may deter investors from investing in New Zealand.
- 41 **Note** that in November 2019, Cabinet agreed that the Minister would be empowered to publish guidance on the operation of the national interest test to manage these risks.
- 42 **Agree** that the Minister publish guidance on the types of matters that will always be considered when assessing a transaction's consistency with the national interest.
- 43 **Agree** that these matters will include:
- 43.1 whether the investment poses risks to national security, public order and international relations (the security and intelligence agencies are responsible for providing advice on national security matters to the regulator),
 - 43.2 whether the investment results in the acquisition of a natural monopoly or other business with significant market share,
 - 43.3 the investment's likely economic and social impact,
 - 43.4 the investment's alignment with New Zealand's values and interests and broader policy settings, and
 - 43.5 the character of the investor, including whether it is a foreign government investor.
- 44 **Agree** that the government publicly note that, for the duration that the COVID-19 pandemic and its economic aftermath continue to have a significant impact in New Zealand, it will also always consider whether the target business is in financial distress.
- 45 **Agree** that this guidance be published at the same time as the Emergency Measures Bill is introduced into Parliament.
- 46 **Authorise** the Minister of Finance and the Associate Minister of Finance (Hon Parker) to refine the national interest considerations, where necessary over time.

Managing transactions during an election period

47 **Note** that urgent decisions under the Act will need to continue to be taken during the 2020 General Election period and following the General Election.

48 **Note** that following the election and before a government is formed, in accordance with the caretaker convention:

48.1 Ministers (or the regulator under delegation) can continue to make decisions under the Act, but

48.2 significant decisions (for example, decisions to block a transaction on national interest grounds) will be made in consultation with other political parties or on the advice of the incoming government (as relevant).

International implications

49 **Note** that the emergency notification power may reduce New Zealand's attractiveness as an overseas investment destination.

[1] [36]

Financial Implications

[1]

53 **Note** that there is uncertainty around the volume of transactions that will be notified under the emergency notification power.

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Legislative implications

57 **Approve** the Emergency Measures Bill for introduction.

58 **Agree** that the Government propose that the Emergency Measures Bill:

58.1 be introduced to the House on 14 May 2020 and complete its first reading the same day under urgency,

58.2 be referred to the Finance and Expenditure Committee for consideration and report back by 25 May 2020,

[33]

[33]

59 **Approve** the Other Measures Bill for introduction.

60 **Agree** that the Government propose that the Other Measures Bill:

60.1 be introduced on 14 May 2020, complete its first reading shortly after that and be referred to the Finance and Expenditure Committee for consideration, and

60.2 be enacted by within 12 months of introduction.

61 **Agree** to give effect to the proposals in this reform package by making amendments to the Act, the Regulations, and any other legislation requiring amendment as a result of the changes proposed in this Cabinet paper.

62 **Authorise** the Associate Minister of Finance (Hon Parker) to make decisions on any additional policy or drafting issues that arise during the implementation of the Emergency Measures Bill and Other Measures Bill, and the Regulations including minor technical changes, in consultation with relevant portfolio Ministers as necessary.

Authorised for lodgement

Hon David Parker
Associate Minister of Finance

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Appendix 2: Proposed guidance on the national interest test

1. This appendix sets out draft guidance on the factors that the Government will consider when determining whether a transaction is, or is not, contrary to the national interest. Where a transaction is found to be contrary to the national interest (which is not defined in the Phase Two Reform Bill), Ministers would have broad discretion to impose conditions on, or where conditions would not be sufficient, prohibit investments to mitigate any risks.
2. This test will apply to certain investments ordinarily screened under the Act that warrant greater scrutiny, such as investments in strategic business or where it grants control to a foreign government. The test will also apply to other transactions ordinarily screened under the Act, as well as notifications received under the emergency power, on a case by case basis where it is considered that these transactions could be contrary to the national interest.
3. This guidance is designed to provide certainty for investors about New Zealand's foreign investment policy, how the Act operates, and whether their investments will be allowed to proceed. Guidance on the types of matters to be considered as part of the national interest test will also support the OIO and other agencies when providing advice on specific transactions.

New Zealand's foreign investment policy

4. The New Zealand government welcomes sustainable, productive, and inclusive overseas investment. Overseas investment supports job creation, the creation and adoption of new technologies, increases human capital, and grants New Zealand more diverse international connections, including access to global distribution networks and markets. Without foreign investment, New Zealanders' living standards would be lower.
5. At the same time, the Government recognises that foreign investment can pose risks. Foreign 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 should own or control those assets. It can also, in extreme cases, present opportunities to undermine our national security.
6. The Overseas Investment Act 2005 (the Act) is New Zealand's principal tool for regulating foreign investment. It seeks to balance the need to support high-quality investment, while ensuring that the government has tools to manage risks. The Act does so by providing an enduring framework for screening foreign investments in sensitive assets to help ensure that they benefit New Zealand and are consistent with New Zealand's national interest.
7. This information is general in nature and is not a substitute for legal advice. Foreign investors should ensure that they understand New Zealand's foreign investment screening regime and ensure they comply with the law, or risk the imposition of significant penalties.

How the Overseas Investment Act 2005 operates

8. The Act requires overseas persons³¹ to get consent before acquiring sensitive land,³² 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.
9. The test that the overseas person must satisfy to obtain consent depends on the type of sensitive asset being acquired. In general terms, if:
 - 9.1 Significant business assets are being acquired, the overseas person must satisfy the investor test, which focuses on the characteristics of the overseas person.
 - 9.2 Sensitive land is being acquired, the overseas person must satisfy the investor test and the benefit to New Zealand test, which requires the overseas person to deliver certain benefits to New Zealand, unless:
 - 9.2.1 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
 - 9.2.2 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.
 - 9.3 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.
10. As of May 2020, all investments in sensitive assets (excluding investments in residential but not otherwise sensitive land) are also potentially subject to review under the national interest test. This backstop test ensures that investments are in New Zealand's national interest, with the New Zealand government committed – where possible – to working with investors to ensure that the national interest is protected. It will always apply to investments in strategically important business assets and investments with a significant foreign government interest, but may also be applied to other transactions at Minister's discretion. Additional information on this test is provided below.
11. From May 2021, investments in strategically important business assets, where consent would not normally be required (for example, because the business is worth less than \$100 million), may be subject to review under the national security and public order call in power. These are referred to as 'call in transactions'.

³¹ Broadly speaking, non-New Zealand citizens and resident, and bodies corporate, trusts and other unincorporated entities that are 25 per cent or more owned or controlled by overseas persons.

³² This includes non-urban land over five hectares, residential land and lifestyle land, and land adjoining sensitive areas such as the foreshore.

12. The national security and public order call in power – expected to be rarely used – allows the government to block, impose conditions on, or order disposal of call in transactions that pose a significant risk to New Zealand’s national security or public order. Additional information on this power is provided below.
13. The Act applies to all overseas persons irrespective of their country of origin and the Overseas Investment Office (‘OIO’) is the Act’s regulator. It makes decisions on some applications and advises decision-making Ministers on others.

The national interest test

14. The national interest test is a ‘backstop’ tool to manage significant risks associated with transactions reviewed under the Act (except for call in transactions). It will be used rarely and only where necessary to protect New Zealand’s core national interests. The test’s, and the Government’s, starting point is that investment is in New Zealand’s national interest.
15. Applying the test means that the Minister responsible for the Act (ordinarily the Minister of Finance) can consider the potential risks of a transaction to New Zealand’s national interest when deciding whether to grant consent. If a transaction is determined to be contrary to the national interest, consent may be declined, or conditions imposed to mitigate any risks. This test will always apply to investments that warrant greater scrutiny:
 - 15.1 where a foreign government or its associates would hold a 10 per cent or greater interest in the asset,
 - 15.2 investments that are found to present national security risks, and
 - 15.3 investments in certain specified strategically important industries and high-risk critical national infrastructure. That is:
 - 15.3.1 significant ports and airports,
 - 15.3.2 electricity generation and distribution businesses,
 - 15.3.3 water infrastructure (broadly, drinking water, waste water, storm water networks, and irrigation schemes),
 - 15.3.4 telecommunications infrastructure,
 - 15.3.5 media entities that have an impact on New Zealand’s media plurality,
 - 15.3.6 entities with access to, or control over, dual-use or military technology,
 - 15.3.7 critical direct suppliers to the New Zealand Defence Force, Government Communications Security Bureau and the New Zealand Security Intelligence Service,
 - 15.3.8 systemically-important financial institutions and market infrastructure (for example, payments systems), and

15.3.9 any other category of strategically important business assets prescribed in the Overseas Investment Regulations.

16. In rare cases, the Government could apply the national interest test to other investments that pose material risks. This would be at the discretion of the Minister responsible for the Act and, if a decision was taken to apply the test, investors would be notified as soon as possible. Potential factors that could trigger escalation to the national interest test include:
- 16.1 foreign government or associated involvement that is below the 10 per cent threshold, but granted that government (and/or its associates) disproportionate levels of access or control to sensitive New Zealand assets,³³
 - 16.2 investments that would grant an investor significant market power within an industry or result in vertical integration of a supply chain, and
 - 16.3 potential inconsistency with Government objectives, for example environmental or economic objectives.
17. Additional detail on what constitutes strategically important business assets can be found in the Regulations.

How the national interest test is applied

18. The national interest, and what would be contrary to it, is not defined in the Act. Instead, the Act grants the Minister responsible for the Act broad discretion to decide on a case-by-case basis whether a prospective investment would be contrary to the national interest. This has significant advantages over a more rigid test, that, for example focussed on investments in certain assets or asset classes. In particular, it:
- 18.1 allows New Zealand's interests to be protected, without establishing a framework that would likely result in valuable investments being declined, and
 - 18.2 ensures that the Act is an enduring piece of legislation that can easily respond to changes in the global risk environment, community concerns about foreign investment, and government priorities.
19. In applying the national interest test, the Government considers a range of factors, the relative importance of which can vary depending on the nature, and likely impact, of the investment. For example:
- 19.1 Investments in large businesses, businesses that have significant market share, or businesses that hold unique assets or operate in particularly sensitive areas of the economy (such as, dual-use or military technology, the health sector, and other critical national infrastructures) may raise more national interest concerns than investments in other types of businesses.

³³ Disproportionate access to, or control, can include: access to non-public information, membership or observer rights on the board, the power to control board composition, and any involvement other than through the exercise of ordinary voting rights in the target entity's decision making.

19.2 Investments that enhance economic prosperity by, for example, increasing New Zealand's productivity, bringing in new technologies, or creating jobs, are less likely to be contrary to New Zealand's national interest.

20. Across all investments, however, there are a number of factors that are generally considered when determining whether an investment is contrary to New Zealand's national interest:

20.1 *National security, public order and international relations:* The Government considers the extent to which investments pose risks to New Zealand's national security, public order, or international relations. Any assessment of national security is informed by advice from the New Zealand Security Intelligence Service, Government Communications Security Bureau, and on public order risks by other agencies where relevant (for example, the Ministry of Culture and Heritage in respect of transactions in the media sector). Advice on international relations is provided by the Ministry of Foreign Affairs and Trade.

20.2 *Competition:* Diverse ownership within and across sectors supports competition and economic growth. In assessing a prospective investment, the Government therefore considers whether an investment may grant the investor market power either within New Zealand (for example, significant market share in one business segment or ownership of a vertical supply chain) or globally (if, for example, an investment may allow an investor to control the global supply of a product or service).

This assessment is entirely separate to any prospective investigation of any transaction by the Commerce Commission, which enforces competition laws and has regulatory responsibilities in a number of specific sectors. This reflects the Act's specific purpose and objectives.

20.3 *Economic and social impact:* The Government considers an investment's likely impact on the New Zealand economy and society, and the extent to which any benefits to New Zealand are commensurate with the sensitivity of the asset being acquired. The benefit to New Zealand test, which provides a formal framework for this kind of assessment in respect of sensitive land, serves as a guide for the types of matters the Government is likely to consider when considering the economic and social impact of investments in business assets.

Additional detail on the benefit to New Zealand test can be found on the Land Information New Zealand website.

20.4 *Alignment with New Zealand's values and interests, and broader policy settings:* The Government will consider the extent to which an investment supports broader Government priorities and policy settings and New Zealand's values. This includes considering an investment's alignment with the Government's economic plan, such as whether it will support thriving and sustainable regions or New Zealand's transition to a clean, green and carbon neutral economy.

Character of the investor: The investor test is the government's primary tool for determining an overseas person's suitability to invest in New Zealand. However, that test is carefully calibrated to minimise that test's burden on the average investor and therefore focussed on the types of risks most likely to be relevant to most prospective investors. The national interest test grants the

Government broader discretion, where necessary, to assess an investor's character and determine whether they are likely to comply with New Zealand's laws, including the conditions of the Act, or whether they have any characteristics otherwise rendering them unsuitable to invest in New Zealand (for example, are subject to international sanctions).

21. For the duration that the COVID-19 pandemic and its associated economic effects continue to have a significant impact in New Zealand, in applying the national interest test, the government would also consider whether the target business is in financial distress. In addition to supporting their shareholders and employees, many New Zealand businesses support New Zealanders' wellbeing more broadly through, for example, their intellectual property, supply-chain linkages, or international connections. The foreign acquisition of such businesses at prices that deviate from their fundamental pre-COVID-19 valuations and risk the loss of these positive externalities may therefore not be consistent with New Zealand's national interest. Wherever possible the Government remains committed to such investments proceeding, with or without conditions, to ensure business viability.

Assessing foreign government investors

22. Consistent with foreign investment screening regimes in comparable jurisdictions, foreign government investors and their associates are also covered by the national interest test as follows:
 - 22.1 all investments ordinarily screened under the Act that would result in a foreign government or their associates holding a 10 per cent or greater interest in sensitive New Zealand assets are always subject to the national interest test, and
 - 22.2 foreign government involvement at lower levels, but where that investor has disproportionate access or control to sensitive New Zealand assets, may be a factor that triggers the discretionary application of the national interest test.
23. In assessing whether a foreign government investor poses risks to New Zealand's national interest, the Government will generally consider:
 - 23.1 the extent to which the investor operates on an arm's length and commercial basis from the relevant government (entities operating at arm's length from the relevant foreign government are likely to pose fewer risks),
 - 23.2 the investor's governance arrangements and prospective governance arrangements for the relevant investment,
 - 23.3 the existence of any other shareholders or partners in the investment,
 - 23.4 whether the target entity will be, or will remain, listed on a New Zealand financial market (additional regulations that apply to listed entities mean that investments in listed entities are generally less likely to pose significant risks),
 - 23.5 the extent to which the investment would grant the relevant government control over, or access to, the underlying asset (for example, investments with no

control rights are less likely to pose risks than those that grant a foreign government significant control of strategically important business assets), and

- 23.6 the share of the entity that would remain owned by non-associated investors if the transaction was to proceed (transactions where non-associated investors will retain a significant degree of control are less likely to pose national interest concerns).

Appendix 3: Proposed split of agreed Phase Two reforms between the urgent Emergency Measures Bill and the non-urgent Other Measures Bill

- Table 2 details the reforms I propose to be included in the urgent Emergency Measures Bill and their commencement timing. Table 3 details the remaining aspects of the Phase Two reform that I propose be included in the non-urgent Other Measures Bill .

Table 2: Reforms proposed to be included in the urgent Emergency Measures Bill

| Provision/reform | Justification | Commencement |
|--|--|---|
| <i>Reforms from Phase Two reform Bill</i> | | |
| National interest test and definitions of strategically important businesses | Necessary to respond to economic and security risks in depressed economic environment. | Two weeks after Royal Assent |
| Call in power and related national security and public order management tools, including information sharing. | Necessary to respond to security risks in depressed economic environment. | Two weeks after Royal Assent, except for powers for the government to review and obligations on investors to notify call in transactions. |
| Enhanced enforcement powers | Necessary to respond to economic and security risks in depressed economic environment. | Two weeks after Royal Assent |
| New Ministerial delegation provisions | Support operation of the above (and new temporary emergency power for transactions worth less than \$100 million). | Two weeks after Royal Assent |
| Protection of classified security information. | Support operation of the above (and new temporary emergency power for transactions worth less than \$100 million). | Two weeks after Royal Assent |
| New investor test (but not repeat investor process) | Streamlines low risk investments to support resilience and recovery. | 12 months or by Order in Council |
| Remove Sensitive Adjoining Land | Removes low risk investments from consent requirements to support businesses. Sensitive adjoining land accounts for around 16 per cent of all consent applications and removing these transactions from the Act will support businesses raising capital and the regulator in prioritising its resources. | Two weeks after Royal Assent |
| Clarify periodic leases don't need consent | Removes low risk investments from consent requirements to support businesses. | Two weeks after Royal Assent |
| Change definition of overseas person | Removes low risk investments from consent requirements to support businesses. | Two weeks after Royal Assent |
| Change 'tipping point' for investments in listed entities | Removes low risk investments from consent requirements to support businesses. | Two weeks after Royal Assent |

| Provision/reform | Justification | Commencement |
|--|---|--|
| Exemption making powers | Critical to ensuring that low risk transactions (such as Residential Mortgage Obligations – a RBNZ regulated securitised asset) and low risk entities can be exempted to support resilience and recovery. | Two weeks after Royal Assent (with new exemptions to be included in Regulations) |
| <i>New COVID response reforms</i> | | |
| Temporary emergency power | Necessary to respond to economic and security risks in depressed economic environment. | Two weeks after Royal Assent |
| Timeframes for emergency power | Support implementation and investor confidence with introduction of emergency power | Two weeks after Royal Assent |
| Exemption making powers for low risk transactions (loans and securitisations) | Necessary to respond to economic and security risks in depressed economic environment. | Two weeks after Royal Assent (with new exemptions to be included in Regulations) |
| Temporary regulation making powers | Necessary to respond to economic and security risks in depressed economic environment. | Two weeks after Royal Assent |

Table 3: Reforms proposed to be included in the non-urgent Phase Two Reform Bill

| Provision/reform | Justification |
|---|---|
| Farmland advertising | More rigorous requirements will likely result in transaction delays. More broadly, these changes do not respond to particular COVID-19 risks. |
| Heightened consent criteria for farmland | These changes do not respond to particular COVID-19 risks. Also, these provisions are already largely achieved through the Ministerial Directive Letter. |
| Enhanced tax disclosures with applications to acquire significant business assets | Serves as a potential disincentive to investment in New Zealand. More broadly, these changes do not respond to particular COVID-19 risks. |
| Special land changes (that is, the Crown's acquisition of fresh and seawater areas) | Serves as a potential disincentive to investment in New Zealand and is likely to delay transactions that include 'special land'. More broadly, these changes do not respond to particular COVID-19 risks. |
| Minor and technical amendments to provisions relating to consent requirements for residential land | Does not address particular COVID-19 risks. |
| Benefits test changes (and analogous changes to Fisheries Act) | Does not respond to particular COVID-19 risks. |
| Repeat investor process | Significant operational change needed to introduce new process. Not required to respond to COVID-19 risks. |
| Remove short term leases | Significant complexity associated with new rules place additional burden on investors and have greater risk of transitional issues. |
| Timeframes for ordinary consent applications | Due to increased volumes, more difficult to meet during COVID-19. Also not scheduled to come into effect until one year post Royal assent, reducing case for urgency. |

Appendix 4: Emergency Measures Bill

Appendix 5: Other Measures Bill