SUBMISSION FORM

Have your say on the Overseas Investment Act 2005

Background

The New Zealand Private Capital Association, Inc (formerly known as the New Zealand Private Equity and Venture Capital Association, Inc) (*NZPCA*) is a not-for-profit industry body committed to developing the venture capital and private equity industry in New Zealand. Its core objectives include the promotion of the industry and the asset class on both a domestic and international basis and the development of a world-best venture capital and private equity environment for the benefit of investors and entrepreneurs in New Zealand.

Our members include venture capital and private equity investors, financial organisations, professional advisors, academic organisations and government or quasi-government organisations.

We welcome the review of the Act currently being undertaken. We comment below on the areas of reform that we consider most relevant to the interface of our members with the Act, principally as vendors and purchasers of assets in respect of which consent is required under the Act, and otherwise as recipients of foreign investment.

Reform of the Overseas Investment Act 2005: Facilitating productive investment that supports New Zealanders' wellbeing

Submission Form

Details of submitter

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Confidentiality request

If you want all or part of your submission to be kept confidential and not uploaded onto the Treasury's website, please mark the applicable box below:

Entire submission confidential	N
Part of submission confidential[1]	N
Name only confidential	N

[1] The text that you do not want published must be clearly marked in the submission.

Responses to consultation questions

1. Sensitive adjoining land (p. 20)

Do you agree that there is a problem, and

- if so, has this paper described it accurately? Can you tell us about your experience, including when it happened?
- if not, do you support the existing arrangements. If so, why?

We agree that there is a problem in that the current definition of sensitive adjoining land is overly broad. We consider that there are sufficient other regulatory mechanisms (such as the Resource Management Act 1991 (*RMA*)) to protect adjoining land and that the Act contributes little in the way of additional protection.

For example, consent could be obtained to acquire land that is sensitive because it adjoins property that includes a listed historic place on the basis that the acquisition would provide an increase in jobs and investment for development purposes – neither of which bear any relationship to the historic place on the adjoining land. There is no clear policy reason why this land is caught by the Act given its use can be regulated via the RMA.

Do you have any comment on the potential effects of the options? Are you able to quantify potential effects on compliance costs?

We anticipate that Option 1 (our preferred option) will result in a material decrease in compliance costs, because identifying sensitive land will be simpler (resulting in lower professional service fees). The saving could be in the order of thousands of dollars per transaction, though this will vary depending on the number of parcels of land in which the relevant acquisition target has an interest.

Do you think the right reform options (pp. 22 – 23) have been identified, and:

- if so, which of the options identified do you prefer and why?
- if not, what alternative option would you support and why?

We think that, of the two options Treasury has proposed, Option 1 better resolves the problems with the current definition of sensitive land. Removing Table 2 land (with the exception of foreshore or lakebeds and land that is significant for Maori) from the definition of sensitive land narrows this definition in a material way, while still retaining exceptions to protect adjoining land where needed.

Alternatively, adoption of Option 2 would still be a significant improvement to the current Schedule 1 to the Act. In particular, we support removing the section 37 'list' land from Table 2. The 'list' is difficult to interpret and apply and there is no clear policy reason for it. The section 37 'list' artificially distinguishes between reserve/public and open space land for no apparent policy reason. We are aware of cases where properties have been assessed as sensitive, where a district plan requires provision of an esplanade reserve, but only upon future subdivision.

9. Screening the impacts of investment (p. 60)

Do you agree that there is a problem, and

- if so, has this paper described it accurately? Can you tell us about your experience, including when it happened?
- if not, do you support the existing arrangements. If so, why?

Treasury has accurately identified the problems with the current benefit to New Zealand test. It is unclear and unnecessarily complex, without accurately capturing instances where an investment may pose a risk to national security.

In our view a test of this importance should properly be developed through the parliamentary process, rather than, as is currently the case, emerging out of a court ruling (the so-called "Crafar farms" decision) where the broader implications of the Court's decision could not be expected to have been considered.

We agree that the current screening of the impacts of overseas investment is cumbersome. Applications for consent become very repetitive as the 21 different factors considered are addressed when in reality there are a limited number of factors that are most important to the decision.

Do you have any comment on the potential effects of the options? Are you able to quantify potential effects on compliance costs?

The scope of factors that must be considered and the complexities of the current counterfactual test add significant time and cost to the process of preparing and submitting an application and to the OIO's consideration of applications. A refinement of the benefits test and/or the introduction of a national interest test should hopefully reduce these costs. Option 1 would add further compliance costs and complexity.

Do you think the right reform options (pp. 67 – 76) have been identified, and:

- if so, which of the options identified do you prefer and why?
- if not, what alternative option would you support and why?

Provided that the issues with the counterfactual test are addressed, we prefer Option 3, being a refined benefit to New Zealand test with the overlay of a national interest test (to apply to a clearly defined set of applications). A simplified benefits test would address many of the concerns with the current screening methods while still allowing for certain decisions to be dealt with by the OIO under delegation, driving timely decisions.

We are broadly in support of the simplified benefits test proposed at paragraph 202 of the Consultation Paper. We would like to see more specificity in the types of economic benefits that will be considered, for example:

- the additional capital value realised by the seller as a result of the foreign buyer's willingness to pay more

- the ability of New Zealanders to raise capital in international markets; and

- greater liquidity for significant assets, which reduces barriers to entry and exit and therefore promotes investment.

Factors of the kind identified above are particularly important in respect of well-run New Zealand assets. New Zealand vendors of such assets are disadvantaged by the current benefits test. In our members' experience, it is often more challenging to obtain consent for a well-run asset, as compared to a poorly-run asset, because of the lesser potential for improvement. Overseas buyers therefore have less scope to demonstrate they will bring the fresh benefits required to receive consent. Ultimately this creates a constraint on liquidity, which potentially deters investors (whether domestic or overseas) from investing in assets that have been well managed or that they intend to develop to a mature state.The national interest test and when it may apply should be clearly defined to give investors as much certainty as possible. It would be a material step backwards for the efficiency and international reputation of the regime (and for New Zealand's reputation as a destination for foreign investment) if a national interest test simply allowed Ministers unfettered discretion over the making of investments.

We consider that Option 3 should be designed to allow Ministers to approve transactions considered in the national interest but not otherwise necessarily meeting the requirements of the simplified benefit test. Likewise it should allow a veto right if a transaction that meets the benefit test is not otherwise considered in the national interest. However, it should not be incumbent on an applicant to have to show an investment is in the national interest in all cases when it is otherwise meeting the benefit test.

If Option 3 is adopted, we consider it is essential that the issues with the current counterfactual test are dealt with. We support Sub-Option A, which would result in:

- a status quo counterfactual test (comparing the state of the land at the time of the application with the overseas person's plans).

- a 'no-detriment test' for transactions involving transferring land between two overseas persons, although the revised test this should make it clear that this should also apply (so long as the other requirements are met) to shareholding changes (as well as transfers of land) and transactions where the benefit to New Zealand test had previously been satisfied downstream of the current transaction, or where the investment in New Zealand pre-dated the benefit to New Zealand test.

This is the only option of the various sub-options proposed which would deal with the problems that arise under the current counterfactual test of artificially constructing what might happen with the investment. Further, we note that facilitating transfers between overseas owners under the 'no-detriment test' should provide investors with greater certainty around their ability to exit, which can in turn increase the attractiveness of investing in New Zealand.

Sub-options B and C both still require a theoretical exercise to assess what might occur. Adopting the vendor's continued ownership of the investment as the counterfactual is artificial as the vendor has determined to dispose of the investment.

We think the principal value of a national interest test is to permit Ministers to intervene in circumstances where the investment would result in a benefit to the public, under the benefit test, but there are overriding reasons to decline consent. Accordingly, the national interest test and simplified benefit test should operate discretely. Put another way, a national interest test and

simplified benefit test that cover the same ground will introduce incoherence into the regime as the same considerations will be assessed under two separate tests.

Do you think the right factors have been identified in the simplified benefit to New Zealand test in Options 2 and 3, and:

- if so, why do you think this?
- if not, which other factors do you suggest and why?

The factors proposed in the paper for a simplified benefit to New Zealand test are reasonable and reflect the practical reality of those factors that are generally determinative under the current Act.

Do you agree that the 'substantial and identifiable benefit' threshold for non-urban land over five hectares should be removed from the simplified benefit to New Zealand test in Options 2 and 3? Why/Why not:

We support the removal of the "substantial and identifiable benefit" threshold as it is too subjective in application. The overlay of the national interest test (in appropriate cases) should allow Ministers to ensure sufficient protections are in place for strategically important assets.

Do you think the right industries have been identified as industries of strategic importance in Option 3, and:

- if so, why do you think this?
- if not, which other industries do you suggest and why?

The Consultation Paper discusses certain assets that, by their nature, may require more careful scrutiny under the national interest test. Examples given are interests in strategically important industries or activities such as media, transport, defence and military, and investments in critical infrastructure.

We think it is important that the test is formulated in a way that considers the circumstances of the investor more than the type of asset

Furthermore, we think that the onus of the national interest test should be on the decision maker to identify a reason why the national interest would be harmed by a particular transaction, rather than requiring applicants to demonstrate that the deal would benefit the national interest. There are two reasons for this requirement.

First, the applicant will already have had to demonstrate that the investment results in benefits to New Zealand.

Second, the national interest should operate as a discrete test alongside the simplified benefit test to capture considerations that are not otherwise addressed in the benefit test (for example, national security concerns). It is unreasonable to require applicants to predict and address in advance the matters that might prompt Ministers to intervene on this ground, or to prove the negative. This

approach is similar to the way the test is framed under the Australian legislation, which is that the transaction proceeds unless it is contrary to the national interest.

Any national interest test should have clear and discrete criteria for Ministers to consider. There are two examples given of existing national interest tests, the test from the Outer Space and High-altitude Activities Act 2017 (*OSHAA*) and the test under the Australian foreign investment legislation. We do not think either of these tests are appropriate to adopt in the New Zealand overseas investment context.

Both of the above tests are too broad in their formulation. While the OSHAA test contains some guidance, it ends with a 'catch-all' that provides the decision maker with an undesirable amount of discretion. The Australian test provides minimal legislative constraint for the decision-maker, with national interest being defined only in ancillary guidance by FIRB. While flexibility is desirable to a degree, it is important that these decisions be free from politicisation and uncertainty.

We think that a national interest test should consider national security, international relations and public safety. We support the inclusion of consideration of the extent to which risks can be mitigated by consent conditions or other legislation.

It is also important that the test is formulated in a way that focuses on the circumstances of the investor and not merely the type of asset. The Consultation Paper discusses certain assets that, by their nature, may require more careful scrutiny under the national interest test – e.g., interests in strategically important industries or critical infrastructure and activities such as media, transport, defence and military.

We would not support a view of national interest that effectively precludes overseas investment in certain types of assets. It could result in investments in the relevant types of asset being avoided completely by our members, given the additional potential difficulty in acquiring or divesting such assets. This would not be a positive development from the point of view of fostering a vibrant private capital ecosystem in New Zealand.

The national interest test should require Ministers to demonstrate why the national interest will be harmed with reference to both the asset in question and the identity and circumstances of the investor.

Regard should be had to the formulation and application of similar national interest/national security tests/powers in countries such as Australia (including under the foreign investment regime), the United States and the United Kingdom, where it is our impression that such powers are rarely used and typically only in cases of utmost national interest or national security concerns.

15. Timeframes for decisions (p. 98)

Do you agree that there is a problem, and

- if so, has this paper described it accurately? Can you tell us about your experience, including when it happened?
- if not, do you support the existing arrangements. If so, why?

We agree that there is a problem. The impact of uncertainty in consent timeframes is acutely felt by our members, who need reliable and accurate indications of timeframes in order to make decisions in relation to the timing of acquisitions, divestments and capital raisings.

Do you think the right reform options and sub-options (pp. 99 – 100) have been identified, and:

- if so, which of the options and sub-options identified do you prefer and why?
- if not, what alternative option and/or sub-option would you support and why?

We support prescribed periods for decision making depending on the type of application submitted. These should factor in a period for Ministerial consideration.

What do you consider to be the appropriate timeframes and why?

We consider the timeframes proposed in Option 2 are too long and suggest deadlines (and extension periods) as follows:

- 30 working days for consent applications subject to a national interest or substantial harm test (if adopted) and for consent applications subject to the benefit to New Zealand test (or the modified benefit to New Zealand test), with a possible extension right of up to 20 working days;
- 20 working days for consent applications subject to the investor and bright-line residential tests or special forestry tests, with a possible extension of 10 working days;
- 15 working days for consent applications subject only to the investor test, with a possible extension of 10 working days; and
- 10 working days for consent decisions involving only a bright-line residential test.

We consider these shorter timeframes are appropriate because:

- assuming the other proposed reforms to the Act are adopted, the red tape in the application process should be significantly reduced (e.g. more refined character assessment); and
- the timing for applications of the types described at 1 above would be broadly consistent with the FIRB timing.

In terms of when the timeframes should commence, we support a solution that combines aspects of Sub-Options A and B, whereby the timeline would start immediately an application was received but would be paused if the OIO determined, within the first half of a prescribed period, that

additional information was required. Any subsequent information requests would not affect the deadline.

Based on our proposed timeframes above, we suggest the following specific timeframes:

- 15 working days for consent applications subject to a national interest or substantial harm test (if adopted) and for consent applications subject to the benefit to New Zealand test (or the modified benefit to New Zealand test)
- 10 working days for consent applications subject to the investor and bright-line residential tests or special forestry tests
- 7 working days for consent applications subject only to the investor test, and
- 5 working days for consent decisions involving only a bright-line residential test.

We consider this to be appropriate because:

- assuming a number of the other proposed reforms to the Act are adopted, the red tape in the application process should be significantly reduced (e.g. a more refined character assessment), and
- the certainty delivered by prescribed periods for decision making would be at significant risk of being undermined if any information requests – even if minor in nature – paused the timeline.

Also for the reasons noted above, we are strongly opposed to Sub-Option C, which would pause the timeline any time additional information was required.

Do you agree that consent should be deemed granted if no decision is made within the prescribed time period and, if so, why do you think that?

We agree that consent should be deemed to be granted if no decision is made within the required time period. This would ensure that the timeframes are effective. If the consideration timeframes can simply be extended without consequence, these reforms will likely fail, as previous efforts to improve timeframes have done. The Act would need to prescribe the basis on which consent would be granted, such as on published standard conditions of consent.

We also strongly agree that consideration be given to the OIO's resourcing.

Other comments on the regime?

If you have any other comments on New Zealand's overseas investment regime, please share them with us below:

Treatment of Limited Partnerships

Under the current framework, there is a failure to recognise the passive nature of investments where no control or degree of influence is held, or sought, by limited partners investing through a

limited partnership. We propose that limited partnerships controlled, and majority owned, by New Zealanders should not be screened by the Act. This could be achieved by the addition of a new class exemption. That class exemption would apply to limited partnerships that are (i) controlled by New Zealanders (which would focus on the control and ownership of the general partner(s) of the limited partnership); and (ii) beneficially owned by New Zealanders (ownership for this purpose being more than 50% of the interests in the limited partnership being owned by or on behalf of New Zealanders).

Alternatively, the same outcome could be achieved by amending the definition of overseas person itself, by adding an additional limb that is specific to limited partnerships (and therefore distinct from the body corporate limb of the definition that currently applies, but is more suited to companies). That new limb of the definition would provide that a limited partnership will only be an "overseas person" if:

- the general partner of the limited partnership satisfies the current overseas person definition (e.g. the body corporate test in section 7(2)(c) of the Act if the general partner was a company); or
- an overseas person or persons own 50% or more of the limited partnership interests.

The effect of either approach is to move the point at which a limited partnership is an overseas person from the current 25% beneficial ownership threshold to a more appropriate 50% threshold (given the passive nature of limited partners' involvement in the limited partnership), while retaining the same thresholds for the control of the limited partnership by focusing on the ownership and control of the general partner.