Regulatory Impact Statement: International investment screening

Coversheet

Purpose of Document	
Decision sought:	This RIS supports Cabinet decision making on the core architecture of the international investment screening regime in New Zealand.
Advising agencies:	The Treasury
Proposing Ministers:	Associate Minister of Finance (Hon Seymour)
Date finalised:	27 November 2024

Problem Definition

International investment supports economic growth by financing the gap between national savings and our investment needs, enhancing productivity, and supporting high paying jobs. However, New Zealand misses out on some of these benefits because we have one of the most restrictive FDI screening regimes in the OECD.

There are a number of issues with the Overseas Investment Act 2005 (the Act), including:

- Why we screen, as reflected in the Act's purpose, contains a presumption against investment irrespective of whether an investment triggers any risk factors
- What we screen, as reflected in the Act's scope, is poorly targeted to risk, meaning we screen many low-risk transactions which diverts resources and scrutiny away from those that genuinely prompt concerns
- How we screen, as reflected in the design of the Act's tests, is relatively intensive by default, requiring consideration already managed via other domestic regulation, rather than being tailored and targeted to manage key concerns not otherwise able to be managed.

The Act has also become increasingly complex, technical, and unwieldy due to a proliferation of bespoke pathways, exemptions, and repeated amendments – often designed to realise a range of secondary policy objectives (such as differential treatment for farmland, water bottling, forestry, and housing supply).

While the potential benefits of attracting more international investment are clear, there are also risks that need to be managed. New Zealand is facing a fundamentally more challenging security outlook, and an enduring screening regime is required to manage risks to our national interest that emerge over time.

Executive Summary

The following options were considered for addressing the policy problem:

Option 1: Status Quo

Option 2: Regime Focused on National Security and Public Order

Option 3: National Interest Focused Regime

The Government’s preferred option is Option 3. This option will improve the investment attractiveness of the regime, manage risks appropriately and provide for a flexible regime that can effectively respond to emerging risks.

This option will:

- Reduce costs and screening time for the majority of transactions required to get consent under the Act, leading to an increase in FDI,
- Enhance the ability of the Act to manage risks, including risks to New Zealand's economic security, and
- Have a variety of economic impacts, including financial benefits, benefits for employees and productivity benefits (noting the evidence for some of these effects is mixed).

Broad consultation with stakeholders (such as investors and professional advisors) and the general public did not occur due to significant time constraints. However, feedback from previous engagements and consultations on the Act have informed the development of the policy proposals in this assessment. This feedback has particularly highlighted the difficulties businesses face in working with the Act.

The public will likely have more mixed views on these proposals. Historically these views have included that the regime should manage a very wide range of risks, including risks that are better managed by other domestic regulatory systems, and that there is inherent non-economic value in retaining domestic ownership of certain assets.

Limitations and Constraints on Analysis

While the overarching objective is to attract foreign investment, the Government has specifically commissioned a review of the Act. As such, this reform has been designed to support the coalition government’s priorities, commitments and decision-making principles, including its commitments to:

- amend the Overseas Investment Act 2005 to limit ministerial decision making to national security concerns and make such decision making more timely, and
- retain the prohibition on foreign investors acquiring or speculating in residential property (which will be out-of-scope of this work).

This means that first principles analysis, consideration of other levers including investment promotion, or design of alternative choices was not undertaken. In addition, options were only considered that could be implemented within this term of government.

The desire to introduce legislation at pace also resulted in some limitations and constraints for the overall policy process. In particular, officials have received feedback from key stakeholders on the issues with the Act and how they might be addressed, but consultation on the detailed design proposals was not undertaken. Proposals have, however, been informed by previous consultation rounds and ongoing engagement with key stakeholders of the regime.

Analysis of impacts is based on a high likelihood of increased FDI resulting from the change. This is a reasonable assumption backed up by evidence but cannot be guaranteed as investment screening is only one factor that influences the flow of FDI.

The evidence of the economic impacts of increased FDI is somewhat mixed. There is a large body of evidence identifying positive economic impacts from FDI, but this tends to focus on developing countries. Evidence that includes developed countries is mixed, and New Zealand specific evidence is rare.

There are limits to the extent to which this evidence base can be utilised to assess the impacts on a sectoral basis. That is, the benefits of a more liberal regime may not flow equally across asset types.

There are challenges regarding how risks are considered. The risks screening regimes can uniquely manage – those pertaining to national security and public order, and economic security and resilience – are rare but can have significant impact. They tend to be very difficult to anticipate and assess, making them difficult to evaluate in the context of an impact assessment.

Responsible Manager(s) (completed by relevant manager)

Conor McBride

Manager

International

The Treasury

2 December 2024

Quality Assurance (completed by QA panel)

Reviewing Agency:	The Treasury
Panel Assessment & Comment:	A quality assurance panel of members from the Treasury reviewed the Regulatory Impact Statement (RIS): International investment screening, produced by the Treasury, dated 27 November 2024. The panel considers that it “meets” the Quality Assurance criteria, but with two notable limitations. Scope: The RIS acknowledges that the scope of the options considered is limited by commitments in the Coalition agreement. In particular, the intent to implement changes within this term of Government places constraints on the scope and depth of the options and analysis. Considering a wider set of first order changes would likely identify options that would be more effective at addressing the defined problem. Consultation: users and key stakeholders have not been consulted in the development of these proposals. While policy and implementation risks are somewhat mitigated by consultation undertaken as part of previous reforms, a high quality process would involve consultation with affected parties and implementing agencies, to ensure that any changes are informed by stakeholder input, are deliverable and that the expected benefits will materialise.

Section 1: Diagnosing the policy problem

What is the context behind the policy problem and how is the status quo expected to develop?

New Zealand needs financial capital to meet its large unmet investment needs…

1 Financial capital is essential for economic growth. However, New Zealand's investment needs persistently outstrip the national savings we have available for investment.

2 As our infrastructure deficit shows, important projects are not proceeding, being deferred, or done more slowly – all of which will hinder long-run economic performance. The Infrastructure Commission estimates it will cost $31 billion per year over the next 30 years to meet our infrastructure needs. International capital can help meet these costs and fulfil our economic potential.

…and our poor productivity performance remains persistent

3 Further, New Zealand’s productivity growth has lagged other developed economies since the 1970s. As a result, New Zealanders have lower incomes and lower material living standards than Australians and Singaporeans, for example.

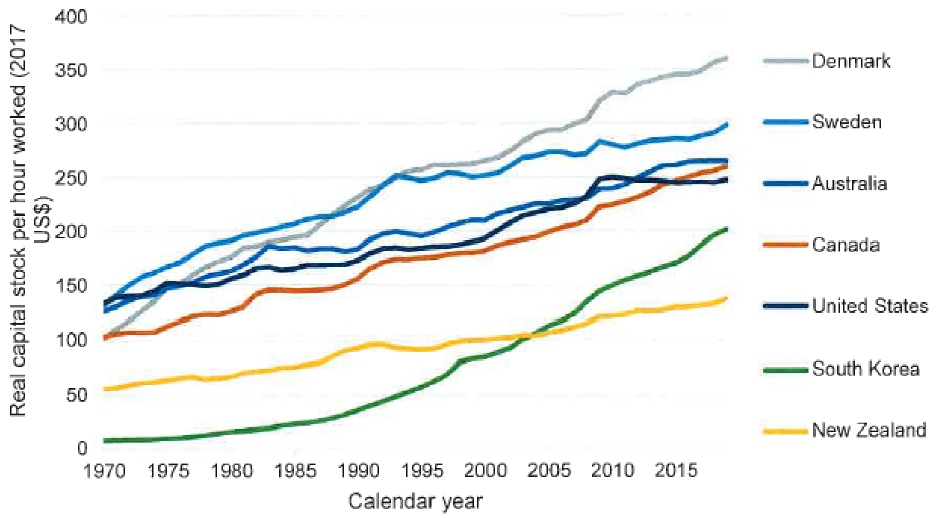
4 The Treasury’s judgement is that there are three drivers are likely to be particularly important in explaining for New Zealand’s poor productivity growth:

a. position as a uniquely small and remote advanced economy (our ‘economic geography’) which contributes to weak domestic competition, limited economies of scale and poor connections to international markets,

b. low capital intensity (refer figure one), and

c. slow adoption of productivity enhancing innovations (for example, firms have been slow to adopt new technology and digital innovation relative to other OECD countries).

Figure one: Capital intensity 1970-2019



International investment is a key lever to improve our economic performance…

5 A range of interventions will be needed to overcome these long-standing challenges. However, attracting foreign investment has a uniquely critical role because it has two distinct economic benefits – namely, it:

a. provides access to global pools of financial capital which will be critical if we are to address our infrastructure deficit, respond to climate challenges, and to support businesses to grow and innovate. New Zealand's national savings are simply insufficient for all these undertakings to be progressed at the scale required to support long-run economic growth.

b. may embody knowledge that helps us to overcome some key productivity challenges (depending on the nature of the investment), and as a result support capital deepening, the diffusion of innovation, and greater competition. The existence of these benefits has strong theoretical support, but (as will be outlined in the impacts section further below) the quantitative evidence defining the impact of these indirect benefits is somewhat mixed.

… but can sometimes pose national security and economic risks…

6 While the potential benefits are clear, foreign investment can also pose risks. New Zealand, like our partners, s6(a) [redacted] Reflecting this the UK, Canada, Australia and the US have all tightened their own investment screening regimes to protect essential security interests in recent years.

7 s6(a) [redacted]

8 The two primary types of risk regard:

a. **National security**. Ownership or control of certain assets, including critical infrastructure (such as electricity or telecommunications networks) and other strategically important businesses (such as media entities or critical suppliers to the defence and security agencies), can provide opportunities for foreign interference, espionage, and sabotage.

b. s6(a) [redacted] In this context, it is important to limit vulnerabilities in our economy to foreign geopolitical leverage and ensure continued access to critical goods and services.

9 Managing these risks is an expectation of the New Zealand public and businesses, [redacted] s6(a) [redacted]. In particular, the US provides regulatory relief for inwards foreign investment from foreign states with robust processes to assess foreign investments for national security risks. New Zealand was granted this status in January 2022 (consistent with the UK, Canada, and Australia).

…and raise significant community concerns

10 In addition to these well-established risks, foreign investment can also prompt community concerns, including whether:

a. there is inherent non-economic value in New Zealand ownership of certain types of land (such as farmland) or 'iconic' businesses,

b. foreign investment has detrimental impacts to the public interest, such as profits 'going offshore' or the loss of jobs to acquiring countries, and

c. the perceived loss of opportunity for New Zealanders to acquire assets, particularly where FDI is likely to have an impact on market value of assets like land.

11 These concerns can become acute, particularly as they are generally concentrated on a single transaction, whereas the benefits of foreign investment are less visible because they are dispersed across the economy.

12 Other community concerns also often arise, such as environmental or other risks. However, these risks arise irrespective of whether activity is financed by foreign or domestic capital. And as such, these risks are best managed by domestic regulatory systems – such as councils' powers to regulate the use of land.

What is the policy problem or opportunity?

New Zealand's approach to international investment screening

13 Given the tension between the economic benefits and potential risks of international investment, most countries regulate it in some way. While such schemes are diverse, they commonly aim to strike a balance between two objectives:

a. Supporting investment attractiveness by minimising regulatory burden and other costs that may discourage the flow of beneficial foreign investment, and

b. Providing appropriate tools to manage and identify risks from foreign investment that are not managed through other regulatory systems.

14 The policy problem or opportunity is to ensure New Zealand gets the balance right between these two objectives, in a form that allows for the regime to respond to a changing environment over time.

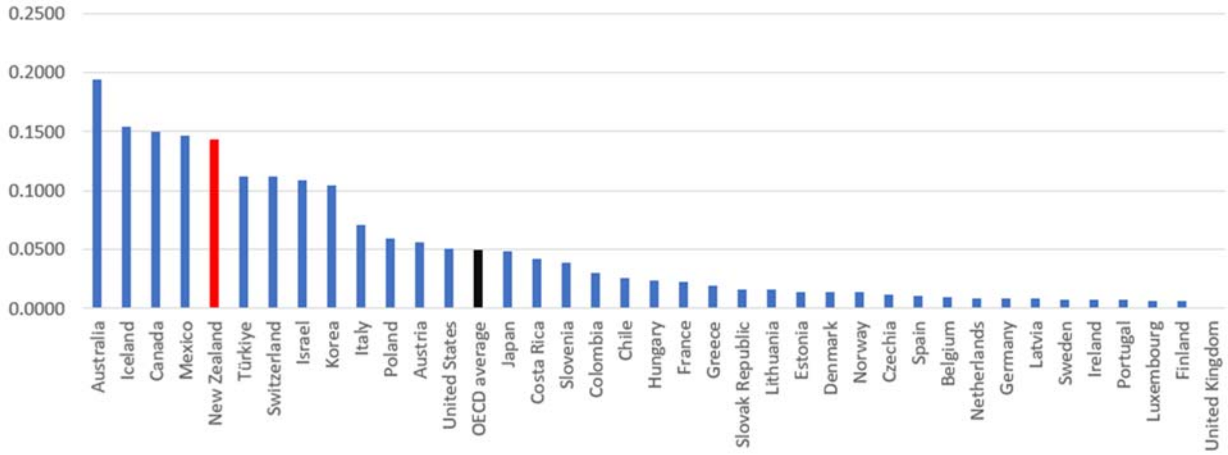
New Zealand's approach is one of the most restrictive in the OECD…

15 There is evidence New Zealand's approach does not balance these objectives well. In particular, the OECD FDI Regulatory Restrictiveness Index shows New Zealand to be highly restrictive of overseas investment. In earlier iterations of the index, New Zealand was found to have the most restrictive foreign investment policy in the OECD. Recent methodological changes find New Zealand no longer the worst (and marginally better than Canada and Australia), but still poor.

16 The index is sensitive to methodology and has some drawbacks suggesting it should only be used as an indicator. The index assesses the scope of screening or design of powers, but does not measure the extent to which those tools are used to block investments (which is generally rare in New Zealand). However, as the presence of such restrictions may limit an investor's willingness to consider an investment in the first place, this indicator remains relevant.

17 OECD work also shows that foreign investment has been persistently lower in New Zealand relative to our peers. New Zealand's total stock of foreign direct investment is approximately 38% of GDP which is lower than the OECD average of approximately 50%.

Figure two: OECD FDI Regulatory Restrictiveness Index (open=0; closed=1)



18 In light of New Zealand's struggles to attract foreign investment, Treasury has assessed the potential role of the Overseas Investment Act 2005 (the Act) is playing. We note that a number of other policy settings (such tax rates, and other regulatory barriers, such as our resource management system) and other factors (the small size of domestic market and remote location) also impact investment flows. This RIA only focuses on the foreign investment screening regime.

19 Treasury has identified three key issues that might be a barrier to foreign investment

19.1 **<u>Why we screen</u>** is reflected in the Act's purpose, which is premised on it being a 'privilege' to invest in New Zealand without acknowledging the benefits investment brings or vendors' property rights. This one-sided purpose statement cascades through to the design of the Act's tests and the regulator's interpretation and administration of them.

19.2 **<u>What we screen</u>** flows from why we screen. The Act's scope is broader than necessary to manage the national security and economic security risks sometimes posed by foreign investment. New Zealand's low ranking on the OECD's restrictiveness index (if updated) would generally result from the 'blanket approach' taken to screening business investments (over $100m) irrespective of the sector. New Zealand also screens all 'non-urban land' over five hectares irrespective of that land's actual characteristics, significance, or monetary value.

19.3 **<u>How we screen</u>** is intensive, duplicates other regulatory systems, and imposes a disproportionate burden relative to the risks that can arise. For investments subject to screening (particularly if land is involved) the default position is 'you cannot invest here, unless…' which is the opposite of most other jurisdictions, including the US, UK, EU and Australia. Alone among our peers, the Act places the onus on investors to demonstrate their suitability to invest here and (when land is involved) they must also demonstrate benefits 'in proportion to the sensitivity of the land.'

…and the Act's complexity is now an issue in itself.

20 The Act has become increasingly complex, technical, and unwieldy due to a proliferation of bespoke pathways, exemptions, and repeated amendments – often designed to realise a range of secondary policy objectives (such as differential treatment for farmland, water bottling, forestry, and housing supply). This suggests the Act doesn't strike the right balance between legislative certainty and flexibility.

21 The Law Society has commented:

> *The principal Act has become very complex and difficult for practitioners to apply and advise on, due to recent amendments…It is respectfully suggested a fresh approach to the principal Act is urgently required, rather than continuing to make piecemeal amendments to the now outdated structure.*

22 Similarly, the Parliamentary Counsel Office advised in 2018 that "*the Act is at the very outer limits of much complexity it can bear.*" The Act has been amended three times since then – twice substantially so, each time adding further complexity.

There are a wide range of pathways

23 There are a wide range of different pathways and tests under the Act, with varying requirements that are inconsistent across different asset types in ways that do not reflect the underlying risk of these transactions. The core tests are:

a. The **Benefit to New Zealand Test**. The Benefit to New Zealand test sets a high threshold for a consent. The Act establishes a framework to determine whether an investment will meet this test, with applications assessed against seven factors (including economic, environmental, access ability, heritage protection, assisting government policy and participation by New Zealanders). There are special variants of the test for farmland and fishing quota.

b. The **Investor Test.** The purpose of the investor test is to determine whether investors are unsuitable to own or control any sensitive New Zealand assets. This test has relatively clear criterial. All consents others than for migrants buying a home to live in are subject to the investor test. Where there are no other sensitive assets, investors in significant business assets only need to meet this test.

c. The **National Interest Test**. The national interest test is a 'backstop' tool to manage significant risks associated with transactions that ordinarily require screening under the Act. It is intended to be used rarely and only where necessary to protect New Zealand's core national interests. The starting assumption for the test is that the investment proceeds unless the government can identify national interest risks.

24 There are also a variety of bespoke pathways, particularly for those looking to purchase residential land but also including existing production forestry.

And high regulatory costs and delays

25 The approach to screening under the Act has led to high fees, additional costs for applicants and long processing times. The application fees vary across the pathways, with the most commonly paid fees ranging from $33,800 to $38,800 and fees for a Benefit to New Zealand application ranging from $68,000 to $141,900. This is on top of other costs such as legal and consultant fees.

26 Lawyers have reported that the Act is complex and that, due to this complexity, legal costs for applicants are expensive – often well in excess of tens of thousands of dollars.

27 It has been previously reported by stakeholders, including New Zealand businesses, investors and legal advisors, that the time taken to reach decisions is long and that ongoing uncertainty, including relating to the possibility of extensions, poses a barrier to overseas investment. Long timeframes can impose delay costs and create uncertainty for investors and other parties with an interest in the transaction, and create challenges for commercial timelines, including the drafting of commercial contracts.

28 The government sought to reduce application processing times by:

28.1 Delegating all decisions that were able to be delegated to the regulator; and

28.2 On 6 June 2024, a Ministerial Directive Letter (MDL) was issued to speed up consent processing times. Improvements in timeframes are outlined below.

29 The delegation letter and MDL illustrated what could be accomplished through improved governance, clear objectives, and risk-based regulation. The delegations and MDL successfully halved application processing times by providing the regulator: increased operational independence; clear investment focused objectives; and a mandate to take a risk-based approach to screening.

30 The Act's purpose statement and the design of the Benefit to New Zealand test limited how much could be done via the MDL. The reforms discussed below are seeking to further these efficiency grains.

31 Consent application timeframes before and after the current MDL are outlined in the following table.

Type of application	Statutory timeframe (days)	Number of applications (12 months pre-MDL)	Average number of days to reach a decision (12 months pre-MDL)	Number of applications (post-MDL)	Average number of days to reach a decision (post-MDL)
Benefit to New Zealand test – general	70	18	66	2	22
Benefit to New Zealand – farm land	100	27	87	11	30
Benefit to New Zealand test – forestry	70	18	123	3	30
Fishing quota	200	0		0	
Residential land development	55	19	40	2	25
Significant business assets	35/55[1]	26	28	5	11
Special forestry test – one off consent	55	23	48	9	19
Standing consent – forestry or residential	100	9	219	0	
Standalone investor test	30	0		0	

Consultation

32 The Treasury consulted with government agencies, including: the Ministry for Foreign Affairs and Trade, Land Information New Zealand, the Department of Prime Minister and Cabinet's National Security Group, the New Zealand Security Intelligence Service, the

[1] 55-day statutory timeframe for when a national interest assessment is also applied.

Government Communications Security Bureau, Te Arawhiti, the Ministry for Business, Innovation and Employment, Te Puni Kōkiri, Parliamentary Counsel Office, and the Ministry for Primary Industries. Some policy proposals were tested with the Legislation and Design Committee.

33 Broader consultation with other stakeholders (such as investors and professional advisors) and the general public did not occur due to significant time constraints. However, feedback from previous engagements and consultations on the Overseas Investment Act have informed the development of the policy proposals in this assessment.

Public consultation in 2019

34 In 2019, the Treasury conducted a public consultation on proposed reforms to the Act. Meetings were also held across New Zealand and in Sydney, Australia with investors, professional advisors, members of the business community, iwi organisations and Māori businesses.

35 The consultation highlighted that the Act's consenting framework is overly complex, and the long processing times and high costs associated with the screening regime resulted in New Zealand assets being carved out of global transactions and being starved of capital. Submitters noted that the benefits test is complex and unpredictable, with the business community noting that the complexity of the benefits test is a key driver of the time and cost involved in obtaining consent.

36 There was broad agreement that there is scope to considerably improve the efficiency of the Act without compromising the Government's ability to manage risks associated with overseas investment, with some suggestion that the screening regime should be framed negatively – that is, there would be a presumption investment could continue unless specific risks were identified.

Consultation with Māori and iwi

37 As part of the Phase Two reform and the consultation on screening settings for forestry conversions, Treasury ran a number of hui with, and received submissions from, iwi and other Māori organisations. Although consultation was on specific proposals, hui and submissions at the time included general conversation on overseas investment screening.

38 Māori and iwi representatives provided a wide range of comments. Some emphasised the value of New Zealand ownership and control, and the importance of ensuring investment benefits New Zealand. Officials also heard that Māori and iwi being able to achieve their aspirations for their land is reliant on being able to access capital, skills, technology and overseas connections.

39 During the forestry hui, some participants questioned the Crown's role in setting the overseas investment rules when Māori entities are involved and considered that the Crown should not be an impediment to 'good' foreign investment, particularly when foreign partners are able and willing to provide capital that could assist in achieving Māori aspirations.

Targeted engagements following the 2021 reform

40 We have engaged with legal firms and experts on their (and their clients') perspectives on the overseas investment regime since it was reformed in 2021. The 2021 reform was largely a targeted reform. It did not, for example, reconsider the 'why' – that is, whether the underlying policy rationale of the Act remains fit for purpose.

41 While the 2021 reform has reduced a lot of unnecessary regulatory burden, these stakeholders noted key issues persist:

a) Even the relatively light-touch screening of significant businesses can contribute to significant legal costs given the number of directors or managers screened under the investor test. Recent streamlining is easily offset when the business has an interest in sensitive land that triggers the more onerous benefit to New Zealand test.

b) A number of major New Zealand firms are screened as overseas persons (notably publicly listed companies) meaning they must regularly apply for consent to purchase assets in New Zealand.

42 The Act has become increasingly complex due to a proliferation of exemptions and amendments to realise a range of ancillary policy objectives (such as differential treatment for farmland, water bottling, forestry, and housing supply).

What objectives are sought in relation to the policy problem?

43 The objectives that effective foreign investment screening regimes must balance include:

a) **Retaining Investment Attractiveness:** regulation must manage risk in a way provides certainty for investors. Regulation must also minimise the regulatory burden and other costs that may discourage the flow of beneficial foreign investment to support economic and productivity growth.

b) **Management of risk**: providing governments effective and efficient regulatory tools to manage risks from foreign investment not managed through other regulatory systems.

c) **Provision of flexibility**: effective regulation of a dynamic sector, such as financial flows, must be designed to provide flexibility to respond to changes in the type of risk or investment flows.

Section 2: Deciding upon an option to address the policy problem

What criteria will be used to compare options to the status quo?

44 We are using three criteria:

- The extent to which **investment attractiveness** is supported, including through reducing the regulatory burden for investors. That is, the regime should be transparent; minimise red-tape, delays, or uncertainties for businesses, vendors, and investors; and integrate efficiently with other regulatory systems.
- The **management of risk** from transactions. This means the government should have targeted and proportionate tools to identify and intervene when an international investment poses risks.
- **The regime is flexible.** It can manage new and emerging risks, as well as facilitating investment to support economic growth. This in turn supports the durability of the regime, by enabling it to evolve without the need for repeated legislative changes.

What scope will options be considered within?

45 Changes to the Act were considered that:

a. Meet the National and Act Coalition Agreement commitment to “amend the Overseas Investment Act 2005 to limit ministerial decision making to national security concerns and make such decision making more timely”, and

b. Maintain treatment of residential land as a sensitive asset (i.e. are broadly consistent with the “foreign buyers ban”).

c. Cabinet’s preference to retain the scope of what is currently screened as s9(2)(h) [redacted]

46 A fuller ‘first-principles’ review was considered, but was identified as infeasible as it could not be completed within the time required and was broader than necessary to meet the coalition commitment. Additional non-regulatory options to attract foreign investment, such as investment promotion, were also not considered in the context of these changes as Ministers commissioned a review of the Act.

47 Further information on how options were developed is outlined in the section below.

Analysis of options

48 Options analysis is outlined in the following sub-sections:

a. High-level options identification and description,

b. Multi-criteria analysis of the high-level options,

c. Analysis of design considerations for the chosen high-level option,

d. Impact analysis of the chosen high-level option and design features.

Identification of high-level options

49 The following questions drove the identification and development of high-level options:

a. **What is the starting presumption?** Should the regime start with the assumption that investment should or should not proceed?

b. **What is the purpose or objective of the regime?** That is, what types of transactions should require approval under the screening framework?

50 Considerations regarding how we screen have largely followed from these choices, as outlined below.

The starting presumption

51 The current purpose of the regime is reflected in the Act's purpose statement, which creates a presumption against investment. This presumption cascades through to the design of the Act's current tests (particularly the benefit test) and the regulator's interpretation and administration of them.

52 Two primary options were considered relating to the starting presumption of the screening regime:

a. **Presumption that investment will not proceed:** Under the status quo the starting presumption in the Act's purpose statement is that it is a privilege to own or control sensitive New Zealand assets. To obtain a consent, investors must demonstrate that the investment is likely to benefit New Zealand and/or meet specific criteria in a bespoke pathway (that is, meet a positive test).

b. **Presumption that investment is allowed:** under a negative test the assumption is that the investment will proceed unless the government can identify risks. Such tests are generally the default for foreign investment screening regimes internationally.

Objectives for why we screen

53 In considering whether there are risks of consenting a particular proposed transaction, the regulator and/or Minister require a test or set of criteria to assess the investment. Officials considered two options relating to why we screen:

a. **National security and public order (NSPO) risks**: Considering only national security and public order risks would narrow the range of risks that are currently considered. The definitions of national security and public order are outlined in more detail below under the description of option 2a.

b. **Whether the investment is contrary to the national interest:** National interest is a broader concept that includes national security and public order. However, National Interest could also include wider factors relating to the economy, risks affecting important social values, or international relations.

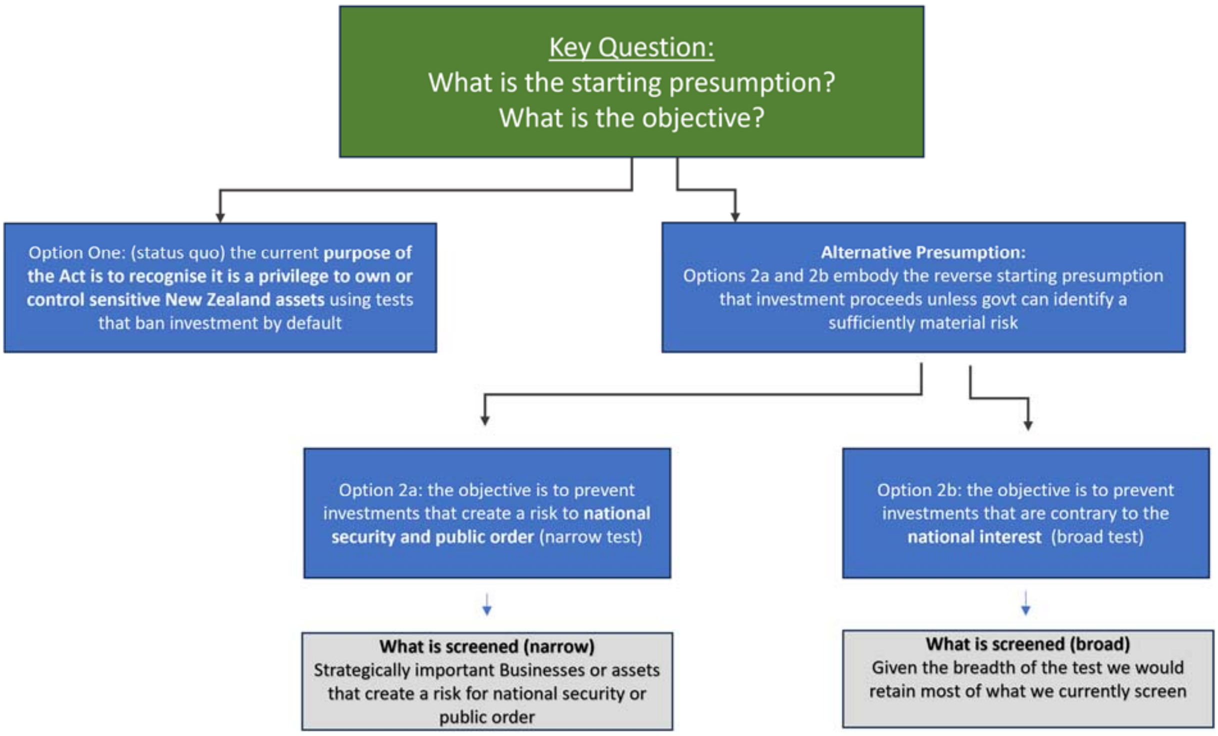
54 The choice between these two options has flow on implications for advice as to what assets should be screened. A narrow focus on national security and public order, for example, would suggest the assets that are screened could have been narrowed to strategically important businesses (SIBs) and a small number of other sensitive security related asset classes.

55 The current regime may be poorly targeted, which gives rise to unnecessary compliance costs for low-risk asset classes. Cabinet chose a broad national interest regime with a clear decision not to change what is screened. As a result, work has not been completed to identify whether New Zealand could stop screening specific assets classes. The question of regulatory burden for lower-risk asset classes has, however, been considered through other design choices discussed within this RIS.

High-level options

56 Answers to the two questions in paragraph 48 above resulted in three high-level options, as per the following diagram.

Figure three: Options relating to presumption and purpose



Description of high-level options

Option 1 – Status Quo it is a privilege to invest (a positive test)

57 Under the status quo the presumption is that investment should not proceed. The purpose of the Act is to recognise that it is a "privilege" to own or control sensitive New Zealand assets.

58 This is implemented through:

a) A default test which places the burden of proof upon the investor who must show that a benefit exists over the status quo (Benefit to New Zealand test), and other bespoke pathways that require specific criteria are met.

Option one: The status quo presumption that investment is banned by default	
Presumption	• It is a privilege to own or control sensitive New Zealand assets
How we screen	• The burden of proof sits with the investor under a positive test • The investor must demonstrate that the investment will or is likely to create a benefit for New Zealand • All transactions must be scrutinised as the regulator must be satisfied that the threshold is met.

Difference between status quo and option 2

59 For the remaining two options (options 2a and 2b), the starting presumption has been reversed to assume that investment should proceed unless a sufficiently material risk exists. This change in presumption creates a negative test that reverses the burden of proof. Under a negative test the government (not the investor) should assess the application and determine whether a risk exists.

Presumption under options 2a and 2b	
Presumption	• Investment should proceed unless a risk exists to suggest it should be declined.
How we screen	• The burden of proof requires the Government to determine whether a risk exists • The regulator can rapidly consent applications with low risk reducing administration and application costs. • High risk applications that are more likely to meet the threshold can be given additional scrutiny.

60 The next two sections consider two different types of risk the Government could screen within a risk-based regime.

Option 2a – managing risks to New Zealand's national security and public order (NSPO)

61 Option 2a would allow investment to occur (a negative test) unless there is a risk to national security and public order (NSPO) risks. It is summarised in the box below:

Option 2a: NSPO Focused Regime	
Why we screen	• To manage national security and public order risks
What we screen	• Strategically Important Businesses • Other assets giving rise to NSPO risks.
How we screen:	• Most investment is not considered by the regulator. Only a small number of investments in narrowly defined sectors are considered likely to give rise to risk.

62 This option would:

- Narrow the purpose of the Act to focus on managing risks to national security and/or public order
- Refine the scope of what investments are subject to the regime to those most likely to trigger concerns from an NSPO perspective

63 The design of the option is based around the OECD's *Guidelines for Recipient Country Investment Policies relating to National Security* ('the OECD Guidelines') and it is similar to regimes in place in other countries, particularly the UK. It would also be based on the existing NSPO screening regime, which screens for NSPO risks which would not otherwise be picked up by the consent regime.

64 NSPO risks can be difficult to define and change over time but include serious threats to one of the fundamental interests of society. Examples include protecting public security, public safety, economic security, and energy security, and combating crime and foreign interference.

65 In addition, screening of some assets would have to conducted in accordance with the security exception or the public order exception in the trade agreement(s) that applies to the investment. s9(2)(h) [redacted]

s9(2)(h) [redacted]

66 The definition for NSPO risks suggests that the assets that should be screened should be narrowed, although a significant amount of work would be required to assess what assets may give rise to NSPO risk. With respect to what is currently screened this would include ‘Strategically Important Businesses (SIBs). SIB categories are defined in the Act, with details established in regulations, and include suppliers to the military, critical infrastructure (including electricity, water and telecommunications companies), and media companies. In 2023, LINZ was aware of 48 investments into SIBs[2].

67 However, if this option were progressed, a review of other asset classes beyond SIBs would have been required to determine whether these assets could give rise to NSPO risks.

Option 2b – managing risks to New Zealand’s national interest

68 Option 2b is also a negative test allowing most investment to occur unless the investments is likely to be contrary to the national interest.

69 National interest is a broader concept that includes national security but may also take into account goals and priorities relating to prosperity and welfare. These can include economic growth, national security, economic security, or cultural values. Identifying risks to the national interest involves balancing the benefits of investment against the risks to the country's future well-being.

70 In practice this test creates a high threshold. But the breadth of the national interest test suggests the regime could continue to screen a broad range of assets. Assets such as fishing quota, for example, may not present a risk to national security, but a depletion of our natural resources would present a risk to the national interest.

71 The features of the option are summarised in the box below:

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[2] This is a combined figure comprising investments in SIBs that required consent, transactions that were notified to LINZ and additional transactions that were identified via monitoring.

Option 2b: National Interest Focused Regime	
Why we screen:	• A balanced framework which recognises that investment generally provides benefits to New Zealand, while also defining that the regime's role is to manage risks to the national interest
What we screen	The current scope of what is screened: • Significant business assets • Sensitive land – non-urban land, residential land and otherwise sensitive land • Fishing quota • Strategically Important Businesses
How we screen	• A rapid triage and assessment process to quickly grant consents to the majority of transactions • A smaller number of applications undergoing thorough assessments

How do the options compare to the status quo/counterfactual?

	Option 1 – *Status Quo Privilege to invest*	Option 2a – Managing risk to NSPO	Option 2b – managing risk to the National Interest
Investment Attractiveness	0	**++** Would substantially increase investment attractiveness as a result of very few restrictions on foreign investment.	**+** Potentially highly attractive due to high bar of national interest test. May create some uncertainty (regarding what is in the national interest) that will need to be managed through guidance.
Risk	0	**-** Addresses most material risks that arise from cross border flows – those relating to national security and public order. Decreases the scope of risks managed by the regime, which puts more weight on domestic regulatory settings better placed to manage 'behind the border' risks (e.g. planning laws to manage development or environmental risks)	**0** (with some probability of **-**) Broad powers to call in transactions to address substantive risks similarly to status quo. However, some risk management would shift to domestic non-discriminatory regulatory regimes.
Flexibility	0	**- -** Very inflexible regime, s9(2)(h) [redacted]	**+** Highly flexible regime. Maintains policy space to reintroduce tighter screening or adopt risk based screening. Shifts some rules from primary legislation to secondary instruments, reducing complexity and providing greater flexibility.
Overall assessment	A wide range of issues as outlined in problem definition.	**+** This option maximises investment attractiveness but limits the ability to address new risks.	**+** This option likely increases investment attractiveness and addresses most risks.

Key:

++	much better than doing nothing/the status quo/counterfactual	0	about the same as doing nothing/the status quo/counterfactual
+	better than the status quo	-	worse than doing nothing/the status quo/counterfactual
+/-	mixed effects	- -	much worse than doing nothing/the status quo/counterfactual

What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

72 Both options 2a and 2b improve the status quo screening regime and would meet the objectives of reform. A presumption towards investment would improve the country's reputation with investors and may boost New Zealand's investment attractiveness. The change in presumption towards accepting investment also provides for a shift towards risk-based regulation. Under risk-based regulation the regulator can target detailed scrutiny towards higher risk sectors or applications to reduce regulatory burden and improve application timelines for lower risk applications.

73 However, the two options contrast substantially in their benefits and, as a result, there are significant trade-offs in these options. The best option depends on the weighting of the criteria.

NSPO (Option 2a) would provide for greater investment attractiveness

74 The reduced focus under an NSPO regime (option 2a) and implied narrowing of what would be screened would have the most significant positive impact on New Zealand's investment attractiveness.

75 A national interest screening regime (option 2b) would also increase investment attractiveness relative to the status quo, albeit to a lesser extent. Shifting the Act's core tests (benefit test and investor test) to a single, negatively framed national interest test would reduce the regulatory burden on investors.

76 A national interest regime would in practice create a high threshold for intervention and is preferable to the status quo. However, uncertainty around what the Government may consider to be contrary to the national interest may negatively impact investment certainty compared to an NSPO regime. Changes in political priorities could also result in 'see-sawing' policy – potentially more so than under current arrangements. The threshold implied by a risk to the 'national' interest and options relating to regulatory safeguards were considered in assessing whether this would reduce investment attractiveness.

77 Options for addressing these risks are considered further in design considerations below.

National Interest (Option 2b) provides for greater ability to manage risk and more flexibility than NSPO (option 2a)

78 Changes in the international security environment and rapid technological advances create a dynamic environment that may raise new risks to New Zealand's national interest. Competition between states, an increase in foreign interference and espionage, and the use of economic coercion have all influenced the risks that may arise from foreign direct investment flows.

79 For this reason, states are increasingly required to consider risks to their economic security alongside risks to the national security. The National Security Strategy defines risks to economic security as actions or developments that threaten the viability of our national economy, including disruptions to critical infrastructure, supply lines, attacks on our financial institutions, and potential economic coercion by foreign states.

80 These risks create a dynamic environment for regulators. The risks are likely to change and the mechanisms by which they may arise are also expected to evolve over the coming years. In response to changes, New Zealand's overseas investment regime

must keep pace with emerging risks and global developments, while still attracting the investment we need to enhance New Zealand's productivity.

81 The limitations of NSPO are that it would:

a) provide more limited tools to manage non-security related risks relating to economic security, and

b) s9(2)(h) [redacted]

82 As a result, the definitions of national security and public order, as contained in international agreements, could limit the ability to address a wider range of risks. However, this risk is partly mitigated by other non-discriminatory regulatory regimes that can manage many of the risks that fall outside of NSPO. As a result, while the uncertainty around the sorts of risks that may arise is high, New Zealand has a lot of regulatory options by which they may be addressed.

83 A National Interest approach (Option 2b) more clearly retains flexibility to respond to risks arising from cross border investment flows. It enables a broader range of risks to be identified and managed, although retaining the scope of what is screened may create uncertainty for investors.

84 Option 2b would allow for risk-based regulation involving targeted scrutiny of higher risk assets classes. While lower risk assets are screened quickly with limited scrutiny, there is no change to what we currently screen. s9(2)(h) [redacted]

Preferred option and further analysis

85 As the Treasury prioritised investment attractiveness, our preferred option is a move to an NSPO regime (option 2a). This judgement is informed by a view that most risks that may arise could be adequately managed by behind the border non-discriminatory regulatory tools.

86 However, as noted, option 2b can also be expected to increase investment attractiveness relative to the status quo while better balancing the other objectives – risk management and flexibility.

87 In addition, in the absence of a full first principles review, it is difficult to fully assess the future risks that may arise from moving to a narrow NSPO regime. The national interest test had clear benefits in that it will better be able to respond to unexpected future risks and/or any limitation on the effectiveness of domestic regulation.

88 For this reason, a more cautionary (i.e. least regrets) approach could support the selection of option 2b. As such, while Treasury did not recommend a national interest regime (option 2b), the choice was not clear cut and our judgement remained finely balanced.

89 As the government proceeded with a national interest focused approach, the rest of the analysis in this regulatory impact statement is on option 2b.

Analysis of design considerations

90 This section outlines analysis of secondary issues (design decisions) for option 2b. The following issues and options are assessed:

Issue	Description	Options
A	Approach to screening investments	• Comprehensive screening of each application to determine whether it is contrary to the national interest (status quo). • Risk based screening – introducing a fast track screening and consenting process for low risk applications and apply a national interest assessment on a case-by-case base.
B	Definition of what may be contrary to the National Interest	• No definition (counterfactual of no further change) • Tight legal definition in primary legislation • High level statutory considerations to illustrate the sort of issues that meet this the national interest threshold • Order in Council Regulations (classes) • Secondary instruments.
C	Delegations and decisions makers:	• Minister alone (counterfactual of no further change) • Power to delegate decision making to the regulator • Mixed approach, with delegated power to consent, but retaining power for Minister to decline consent
D	Capturing investor risk	• An investor test in primary legislation (counterfactual of no further change) • Regulations defining classes of investment that create risk • Investor characteristics included in the GPS
E	Changes to the National Security and Public Order regime	• No change (status quo) • Additional regulation making powers
F	Farmland advertising	• No change (status quo) • Remove the farmland advertisement requirement

91 Options under each issue are assessed against the either the status quo or the counterfactual of no further change.

Issue A: approach to screening (comprehensive or risk based)

92 A move from a positive test (i.e. the benefit test) to a negative national interest test reverses the burden of proof, requiring the Government to identify whether a risk exists. A national Interest test could create similar compliance costs if it were to be applied to every transaction.

93 The first consequential design decision was whether screening through the national interest test should be risk based. The Government has chosen to retain the current regulatory perimeter, suggesting a significant number of low-risk transactions will need to go through the national interest assessment.

94 While the requirements for the current benefits test are clearly defined in legislation, the Act does not define what is "contrary to the national interest". Given greater decision-making power under the national interest test will be vested with the regulator, it will be important for the Government to define which risks it is seeking to manage and the process for screening transactions to reduce the compliance burden for investors.

95 In considering how to screen transactions under the national interest, officials have assessed the following options:

Option A1*:* Comprehensive screening of each application to determine whether it is contrary to the national interest (counterfactual of no further change).

Option A2: Risk-based screening – introducing a fast-track screening and consenting process for low-risk applications and apply a national interest assessment to higher risk applications on a case-by-case base.

	Option A1 (counterfactual)	Option A2 (risk-based screening)
Investment Attractiveness	0 High regulatory burden from applying a national interest test to all applications	++ Most transactions screened under fast track, with few higher risk applications undergoing a full assessment
Risk management	0 Supports risk management through screening all transactions	+/- High-risk applications escalated for national interest assessment, providing for greater focus on risky transactions, but chance for regulatory failure
Flexibility	0 Limited flexibility to change the level of scrutiny of individual transactions	+ Flexibility to define what is high risk and needs further scrutiny on a case-by-case basis

96 Implementing option A1 as part of the preferred high-level option has the potential to create a higher regulatory burden than currently exists. A national interest assessment can be a complex process with high information requirements, which is inappropriate for low-risk asset classes and transactions.

97 Option A2 – the preferred option – would, on the other hand, better balance the need for screening of all relevant transactions and identifying national interest risk, with efficiently consenting low risk transactions. By moving to risk-based assessment, however, the Government will take on some risk of regulatory failure (with applications consented that otherwise would have required a national interest test).

Issue B: Defining what may be contrary to the National Interest

98 National interest creates a high threshold, but interest is an inherently subjective and political concept that may create uncertainty for investors. While New Zealand has a number of enduring national interests (such as addressing risks to our national security), other interests may evolve in response to a number of factors, including international developments and the priorities of the government of the day.

99 The Act does not define what is contrary to the national interest. While this lack of definition means the test can respond to the issues and priorities of the day, it may also create uncertainty. While this was less of an issue when national interest was a backstop power, this uncertainty may become an issue if it were to become the core test in the Act.

100 Investor uncertainty could be addressed in a range of different ways. Detail in the Act or guidance from the government may help reduce this uncertainty. But different instruments have different trade-offs, notably around the degree of flexibility provided. All else equal, a more flexible instrument is more able to respond to new and emerging risks and uncertainty in the external environment.

101 There are a number of options available for the Government in seeking to defining national interest. These include:

Option B1: No definition (counterfactual of no further change)

Option B2: A tight legal definition in primary legislation

Option B3: A set of high-level statutory considerations to illustrate the issues that meet the national interest threshold

Option B4: Order in Council Regulations defining classes of investment that create a risk to national interest

Option B5: Non-legislative secondary instrument, such as a government policy statement (GPS).

	Option B1 (counterfactual)	**Option B2** (tight legal definition)	**Option B3** (statutory considerations)	**Option B4** (Order in Council regulations)	**Option B5** (secondary instruments)
Investment Attractiveness	0 High investor uncertainty	++ Clear threshold for intervention but potential for over capture	+ Supports certainty through providing guidance	+ Supports attractiveness through clarity on what are high risk transactions	++ Communicates to investors the Governments priorities
Risk management	0 Difficult to triage and focus on identified risks	- Lacks flexibility to consider additional risks	+ Better focus of resources on identified risks	++ Enables efficient escalation of emergent risks	+ Directs regulator on risks to focus on specific risks
Flexibility	0 Broad discretion for intervention, but unlikely to support the regimes durability	- Difficult to change definition to match risks and priorities	+ Supports durability through flexibility	++ Maximises flexibility and durability	++ Highly flexible instrument that can be amended with changing priorities

102 Options B1 and B2 present significant issues to the operation of the regime. Having no definition or way of refining national interest under the status quo may create uncertainty and reduce attractiveness. Conversely, while a tight definition in the Act would be a clear steer to investors, it could lead to both over capture of low-risk transactions (if drafted broadly), and regulatory failure by not providing the regulator the flexibility to identify and escalate high risk transactions.

103 Our preferred option is a mix of options B3, B4, and B5:

a. A set of considerations in legislation (B3) illustrate what may be considered in determining whether an investment is contrary to the national interest. The considerations give direction to both investors, the regulator, and Ministers on how the process will operate,

b. Order in Council regulations (B4) mandating the escalation of certain transactions to also provide certainty, while also ensuring that risks from certain classes are always considered, and

c. Other secondary instruments (B5), such as a government policy statement (GPS), are another signal to investors of priorities and risks.

104 Taken together, these options provide clear direction to investors while preserving the flexibility of the regime.

Issue C: Delegation and decisions makers

105 Under the current Act, the national interest test is a backstop test, which allows the Minister to 'call in' a transaction if he/she considers that it may be contrary to the National Interest.

106 The Minister of Finance is responsible for making decisions on both whether an application should undergo a national interest assessment, and on whether to approve, condition, or decline a transaction. The power to decline on national interest grounds cannot currently be delegated to the regulator given the political nature of the test. Decisions made on transactions that are screened under other tests (such as the benefit test) can be fully delegated to the regulator.

107 The following options for the national interest test decisions makers have been assessed:

Option C1: Minister alone can approve or decline consent (counterfactual of no further change)

Option C2: Minister can delegate ability to approve or decline consent to the regulator

Option C3: Mixed approach, with the regulator vested with the power to consent and impose conditions, unless the transaction has been escalated or called in to the Minister. Only the Minister can decline a transaction.

	Option C1 (counterfactual)	**Option C2** (power to delegate all decision)	**Option C3** (mixed approach)
Investment Attractiveness	0 High regulatory burden	+ Improves efficiency of application screening	+ Improve attractiveness through clear thresholds and processes

Risk management	0 Poorly targeted at risk management	- Inappropriate, as Ministers should retain the power to decline transactions under national interest	+ Retains Minister's power to manage national interest risk
Flexibility	0 Inflexible in approach due to high regulatory burden	- Inappropriate delegation of power, given national interests political nature	+ Decisions on risk escalated to the appropriate level

108 While determining whether a transaction is contrary to the national interest is a subjective political judgement, granting consent for low-risk applications that are highly unlikely to present a threat to national interest is not. Given the national interest test will now be the primary test, it would impose a high burden to have all transactions escalated to a Minister for consent, ruling out option C1. Conversely, delegating decisions making for all transactions would be efficient, but would mean that the regulator would be left to decide what is contrary to the national interest, which is an appropriate consideration for Minsters as elected officials.

109 The preferred option is C3, wherein the regulator can approve and condition lower risk transactions that are clearly not contrary to the national interest, but only Ministers can decline transactions. This option balances the need for efficiency in the process, while also ensuring that decisions to decline on the grounds of national interest are taken by the appropriate decision-maker.

Issue D: Investor test

110 This section discusses options for how investor characteristics can be considered as part of a national interest only regime.

111 The Act's current investor test (section 18A) determines whether investors are unsuitable to own or control any sensitive New Zealand assets based on factors relating to their character and capability, for example criminality or unpaid tax. While the test is relatively bright line in nature, criteria, such as imprisonment for five years, are poorly targeted and overly granular. As a result, the test may not capture characteristics that may be relevant to a national interest assessment. For example, while the test screens for serious criminal convictions, investors may have relationships with foreign governments or individuals that give rise to national security risks.

112 In considering how to capture investor risks, the following options were considered:

Option D1: Retain the current investor test in the Act (counterfactual of no further change)

Option D2: Order in Council Regulations defining classes of investment that create a risk to national interest

Option D3: Investor characteristics included in a secondary instrument, in particular a GPS.

	Option D1 (counterfactual)	**Option D2** (inclusion in regulations)	**Option D3** (inclusion in a secondary instrument)
Investment Attractiveness	0 Provides clarity on process but poorly targeted	+ Provides clarity on what characteristics are relevant, but potential for over-use	++ Provides both clarity on characteristics, and flexibility for the regulator
Risk management	0 Does not capture full range of risks	+ Identifies relevant risk factors	+ Identifies relevant risk factors
Flexibility	0 Highly inflexible criteria	+ Flexible, able to be changed without legislative amendment	++ Very flexible, able to be quickly changed

113 The status quo (option D1) is poorly targeted, overly granular, and requires legislative amendment to change, meaning it is poorly placed to respond to emergent risks. Moving detailed criteria from the Act to a secondary instrument would improve flexibility and allow the regime to capture risk.

114 The Treasury's preferred option is D3 – inclusion in a relevant secondary instrument (in this case, a GPS). This will be drafted to provide high-level guidance on government policy. It will provide the best compromise between flexibility and certainty if it articulates principles for investor screening that the regulator could apply through detailed guidance.

Issue E: National Security and Public Order (NSPO) regulation making powers

115 The NSPO regime screens transactions in sectors where overseas investment could have NSPO risks. Transactions with potential NSPO risks are screened in two ways:

a. NSPO risks arising within the core screening regime (i.e., for land, fishing quota, and significant business assets) are called in for screening under the current national interest test, and

b. Investments in strategically important businesses (SIBs) that do not require consent are called 'call-in transactions'. Some of these transactions must be notified by the relevant investor, while for others the investor may notify voluntarily. The relevant Minister *must* review all call-in transactions that have been notified and *may* review transactions in SIBs that have not been notified.

116 The external security environment is increasingly dynamic and uncertain, and while it is difficult to predict with certainty the sectors where NSPO risks may arise, it is likely that new risks will emerge in the future.

117 The current legislative settings for the NSPO regime do not provide sufficient flexibility for the government to be responsive to new, emerging risks. While the Act was amended in 2020 to provide NSPO screening powers, the transactions that must or may be called in are relatively tightly defined.

118 High-level SIB categories are defined in the Act, with regulation-making powers that provide for the prescribing of sub-classes of business that are, and are not, SIBs. This regulation-making power is limited to prescribing SIBs that fit within the existing categories set out in the Act. This means adding a new type of SIB that does not fit within the existing categories requires amendments to the Act.

119 The following options were assessed with respect to adding new regulation making powers for NSPO:

Option E1: No change (status quo)

Option E2: Amend the Act to provide for regulation-making powers to add new categories of SIBs and determine that certain call-in transactions must be notified.

	Option E1 – Counterfactual	Option E2 – New regulation-making powers in the Act
Investment Attractiveness	0 Static regime with SIB definitions provided in legislation and regulations	- Enabling the government to add additional SIBs to the NSPO regime, or to require additional call-in transactions to mandatorily notify the regulator may be seen as adding regulatory burden for investors, thereby reducing overall investment attractiveness.
Risk management	0 Lacks powers to add new classes for escalation	++ This option provides the government the appropriate tools to intervene when required.
Flexibility	0 Changes required to primary legislation to add new classes	++ This option enables the regime to be flexible by enabling the government to respond quickly to new, emerging risks without having to amend primary legislation.

120 Option E2 is preferred. It would provide the flexibility to define new classes of transactions that require escalation, allowing for faster responses to new, emerging NSPO risks.

Issue F: Farmland advertising

121 Before a vendor can sell a farm to an overseas person, they must obtain consent and advertise the property (in a paper publication and on the internet) for thirty working days.

122 The farmland advertising requirement intends to provide New Zealanders an opportunity to make an offer before a sale is made to an overseas person. While vendors may choose to sell direct to a foreign person, many vendors will consider advertising to maximise their sale prices, regardless of the requirement. Ultimately, whether they decide to advertise or not sellers will usually seek the best price regardless of whether the purchaser is local or foreign, making a requirement to advertise an unnecessary regulatory burden.

123 The Act allows responsible Ministers to issue class exemptions which are currently used for a range of circumstances where a farmland advertisement requirement would be

inappropriate. Examples include the sale to related party or situations where there is no effective change in control. Class exemptions can be difficult to target and must be reviewed and reissued periodically. Where a class exemption does not exist, the fee for an individual advertising exemption is high at $13,000.

124 The following options were assessed:

Option F1: No change (status quo)

Option F2: Amend the Act to remove the farmland advertisement requirement

	Option F1 (Status Quo)	Option F2 – (Remove the farmland advertisement requirement in the Act)
Investment Attractiveness	0 Unnecessary regulatory burden	++ Removing the advertisement requirement reduces regulatory burden for investors, therefore increases investment attractiveness.
Risk management	0 No impact	0 The advertisement requirement is not seen as an effective risk management tool as vendors are usually incentivised to advertise to maximise their sale price, regardless of the requirement. Therefore, removing the requirement is unlikely to affect the government's ability to manage risk appropriately.
Flexibility	0 Reduces the flexibility and durability of the regime through unnecessary regulatory burden	+ This option enables the regime to be more durable by removing unnecessary regulatory burden for investors.

125 Option F2 is the preferred option, as this will increase investment attractiveness by removing an unnecessary regulation. Removing the advertising requirement will not impact the regime's ability to manage risk.

Summary

126 To summarise, the preferred design features for option 3 are:

a. Moving to a risk-based screening regime

b. When considering whether the transaction is or is not within the national interest, the following are relevant:

   i. A set of high-level considerations included in primary legalisation

   ii. Regulations which mandate the escalation of classes of investments

   iii. Further definition of national interest and government priorities through a secondary instrument (a GPS)

c. Vesting the regulator with the power to condition and consent applications in most circumstances, but maintaining Ministerial discretion to decline transactions

d. Identifying relevant investor characteristics for national interest assessment in a GPS

e. A new regulation-making power for mandating classes of transactions to be called-in under the NSPO regime, and

f. Removing farmland advertising requirements.

127 This combination of options meets the criteria:

a. **Retaining investment attractiveness:** The regime will minimise regulatory burden through moving to risk-based screening of transactions, and support investor confidence through clearly articulating the process for screening applications, and the areas in which the Government has identified risks.

b. **Management of risk:** high-risk applications will be escalated to a national interest test. Inherently high-risk classes of transactions will be escalated both on a mandatory basis (through regulation) and on a discretionary basis by the regulator (as per policy set out in the GPS).

c. **Provision of flexibility:** The options will improve flexibility through creating powers to add additional classes through regulation for both the national interest and NSPO regime. The GPS will be a tool for both managing risk (such as identifying relevant investors characteristics) and setting government policy towards overseas investment.

What are the marginal costs and benefits of the option?

128 This section considers impacts of the entire package (option 2b plus design features), including:

a. Impacts on screened firms,

b. Likely economic impacts,

c. Risks, and

d. Other relevant impacts.

129 The description of these impacts is largely qualitative, and no formal cost benefit analysis (CBA) has been conducted. A CBA was not possible in the time available, and a comprehensive CBA would depend on the implementation of the changes, including how the Government chooses to further define national interest in regulations and the GPS. There would be further challenges in producing a CBA, particularly with regard to costs. In particular, although some assumed benefits from increased investment could be estimated (albeit with mixed evidence in places), the low likelihood or indirect impact of the costs arising, and their variable nature would limit the utility of quantified comparisons.

New Zealand's reputation and direct impacts for foreign investors

130 Lower compliance costs and faster application processing times for overseas investors will create a direct benefit for investors. The presumption will be that investments must proceed unless a risk can be identified, which will allow the regulator to take a risk-based approach to regulation.

131 Under a risk-based approach, the regulator undertakes little or no screening for assets that are unlikely to ever present a risk to the national interest. For example, a marginal change in aggregate foreign ownership (e.g. from 49% to 51%) for a low-risk company with many investors could now be consented in days.

132 Under the proposed approach most applications should now be able to be approved via fast-track consenting with an ability to escalate transactions for additional scrutiny on a case-by-case basis.

Patterns of Investment

133 This reform maintains the current regulatory perimeter – that is, it does not change what is screened.

134 The regime currently screens sensitive land, significant business assts valued over $100 million (with alternative higher thresholds for other jurisdictions such as Australia where the current threshold is $618 million for non-government investors), and investments in companies holding fishing quota. Strategically Important Businesses that may present a NSPO risk are also screened.

135 In practice, the value of these screened investments may constitute a relatively small percentage of New Zealand's cross border financial flows. The Act currently focuses on ownership or control interests of over 25%. Balance of Payments data suggests that portfolio flows below this control threshold and makes up the majority of investment. FDI was around 30 percent of foreign investment into New Zealand.

136 Previously analysis by Treasury has suggested only a small percent of foreign direct investment also goes through the screening regime, but data discrepancies make comparison between consent and balance of payment data difficult.

Changes in what kind of investment will occur?

137 The impact of this policy will be influenced by the Government's final policy decisions for the proposed GPS. However, notwithstanding this, we expect the most pronounced change will occur in the sectors that are currently most intensively screened.

138 The current screening regime has a dampening effect that is most pronounced for farmland and forestry investments as the Minister must place a higher relative importance on factors relating to local participation and the economic benefit over the status quo. While not impossible, this test may be difficult to meet for farms operating at or near the productivity frontier.

139 As such, the removal of the benefit test could lead to an increase in investment in primary industries. However, this will depend on wider investment conditions and the how the changes are implemented (including, for example, any conditions established in the GPS).

140 The Treasury is assuming that a more investment friendly Act in conjunction with the Government's current focus on investment attraction will increase FDI in significant businesses over time.

141 A substantial increase in business investment may not arise as a direct result of these changes. Significant business investments must only pass the reasonably straight forward investor test, which most investors currently meet. However, the new regime should reduce compliance costs even for these transactions and the signalling effect of a more investment friendly regime should boost New Zealand attractiveness as an investment destination.

Economic impacts

142 The Treasury's views on the economic impacts are informed by the relatively small percent of investments screened by the regime and nature of the assets screened.

143 The impact will depend on government policy (i.e. the GPS), as a result this document only provides an overview of the potential forms of benefit, risk, and potential impact.

An increased likelihood of FDI

144 To increase FDI the Government will need to release guidance to provide investors with certainty. A regulatory chilling effect could occur under a broad national interest test if investors are unclear as to what risks the Government intends to screen.

145 However, given the Government's focus on international outreach and investment promotion we expect that this policy will lead to an increase in FDI over time.

146 Empirical evidence in academic literature supports this assumption. Reduced restrictions are normally associated with a more favourable approach to investment. A survey by the OECD[3] finds that reduced restrictions on FDI lead to an increase in investment. The OECD finds that a change in the FDI Regulatory Restrictiveness Index of 10% (prior to the index's methodological change) increases bilateral FDI inward stocks by 2.1% on average.

147 The Australian Productivity Commission estimated that increasing Australia's restrictions on foreign investment to a similar level of restrictiveness as New Zealand would reduce GNI by between $0.8 and $7.1 billion (or $82– $731 per household per year), due to a loss of $19–$182 billion of net foreign capital.[4]

148 New Zealand must also compete for capital in global markets. The work by the OECD suggests other countries have liberalised since the 1980s. Liberalisation of FDI screening in other countries will have a negative impact on investment in similar countries that have not liberalised (e.g. New Zealand).

Financial and valuation effects

149 An increase in FDI may increase the value of New Zealand assets. The benefit of valuation increases will flow to New Zealand vendors who may receive a higher price on sale.

150 With regard to businesses or productive assets, foreign investment may increase the value of firms and/or provide an exit opportunity for entrepreneurs. The ability to sell part of the business to a foreign investor may encourage entrepreneurs to begin new enterprises in New Zealand.

Foreign direct investment can "enable" economic growth

151 The long-term impact of an increase in FDI on economic growth is ambiguous as:

a. proceeds from the sale of an asset could be invested by the vendor or simply consumed, and

b. to realise the benefits from FDI, New Zealand will need to create high productivity or high-return opportunities for foreign investors to invest in.

152 For this reason, the Treasury see investment screening as enabling change but not guaranteeing it. An increase in FDI is necessary to finance our investment needs but may not be sufficient to guarantee growth. To obtain the full benefits from this reform the Government will need to make supporting changes to planning, tax, or regulatory regimes to create or encourage productive opportunities for investment.

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3 The Determinants of Foreign Direct Investment: Do Statutory Restrictions Matter? https://www.oecd.org/content/dam/oecd/en/publications/reports/2019/03/the-determinants-of-foreign-direct-investment_c371303e/641507ce-en.pdf

4 Foreign Investment in Australia, Australian Productivity Commission, https://www.pc.gov.au/research/completed/foreign-investment/foreign-investment.pdf

Direct financing for growing businesses and/or productive assets such as infrastructure

153 As noted, FDI can fund business investment, infrastructure, or capital deepening. New Zealand's current account deficit is currently 6.7% of GDP. The persistent current account deficits, show that New Zealand's national investment needs have persistently exceeded domestic saving. The Treasury expect investment will continue to exceed domestic savings.

154 FDI can particularly help in financing New Zealand's infrastructure investment. The Infrastructure Commission estimated in 2021 that an additional $104 billion in capital is needed to meet New Zealand's infrastructure needs.[5] In addition to correcting the historical under investment in infrastructure, New Zealand will need to respond to long-term-trends including, an aging and increasing population, and the need to adapt and respond to climate change. New Zealand's physical infrastructure is particularly vulnerable to impacts from climate events and natural hazards.[6]

155 Investors already make a significant contribution to infrastructure investment. Energy (investments worth $8.7 billion in the years 2019 to 2023), communications services (investments worth $14 billion in the years 2019 to 2023) and other utilities have attracted a sizeable proportion of FDI investment from overseas investors in the last decade[7], a trend that can be expected to continue.

156 It is worth noting that, the financial benefits of FDI may eventuate regardless of the asset that is sold. Direct investment in a high growth New Zealand firm will provide a benefit for the economy. But the same benefit arises where a New Zealand investor sells a low return asset (such as land) and uses the proceeds to invest in the same high-growth opportunity.

Impact on Firm Productivity

157 Foreign direct investment can also create a large number of indirect benefits, including:

a. effects on firm productivity,

b. the transfer of technology, knowledge and skills, including enhanced managerial capability and innovative organisational structures, and

c. higher wages for employees.[8]

158 While international evidence supports that benefits arise from strong international connections, statistically significant quantitative evidence making the link between ownership of shares and indicators of productivity is mixed. The quantitative benefits of investment are highest in capital constrained emerging economies, countries further from the productivity frontier, or in countries, such as Ireland, that enjoy geographic proximity to higher-productivity countries.

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[5] new-zealands-infrastructure-challenge-quantifying-the-gap.pdf (umbraco.io)

[6] NZ Treasury (2024), The Productivity Slowdown: Implications for the Treasury's forecasts and projections, Treasury website at May 2024: https://www.treasury.govt.nz/publications/tp/productivityslowdown-implications-treasurys-forecasts-and-projections

[7] As identified by KPMG: https://kpmg.com/nz/en/home/services/advisory/deal-advisory/foreign-direct-investment-in-new-zealand.html

[8] Sanderson and Fabling (2011) find evidence in New Zealand that foreign acquired firms exhibit stronger growth in average wages and average employment than other firms, but that the productivity effect (as measured by wages) did not appear to follow employees transitioning to domestic firms.

159 Quantitative analysis of the productivity impacts of foreign investment in New Zealand has typically not been statistically significant. A range of factors could explain this discrepancy, but one plausible explanation is that foreign investors may be passive, which limits the transfer of management experience or knowledge. While firms with foreign investment tend to have higher productivity, Sanderson and Fabling (2011) found that foreign firms tend to target and invest in higher productivity New Zealand firms.

160 It is worth noting that passive investors still provide a significant financial benefit for target firms. These passive investors provide capital and present a limited risk from a foreign investment screening perspective. To illustrate, Sanderson and Fabling found that target New Zealand firms grow more quickly suggesting a benefit for economic growth, but in general the productivity benefit and/or capital intensity of the domestic firm does not tend to increase[9].

Industry Spillovers

161 A (2014) study by the Ministry of Business Innovation and Employment (MBIE) found that evidence for productivity spillovers was weak, the overall impact of FDI on the New Zealand economy was substantial, even in the absence of spillovers.[10] At that point, foreign firms accounted for a quarter of total employment and almost 40% of sales and value added.

162 The MBIE study found that the impact of foreign investment can have more significant implications for productivity at the industry level. There was a significant positive productivity impact of foreign penetration in downstream industries. An increase in foreign ownership of 1% can increase the productivity of these other firms by 0.86%. This occurs on account of competition, which may have implications for smaller less productive firms.

Economic costs and risks

An increase in foreign control of sensitive assets

163 Foreign control of firms is beneficial providing the firms are managed on a commercial basis with a view to increasing the value of the firm/investment over time.

164 Foreign investment by non-commercial entities such as foreign governments may come with risks if the investment is made for non-commercial or policy reasons. This is a risk that the regulatory screening regime is seeking to manage.

165 Foreign ownership of non-business assets (e.g., residential assets not on residential land) may increase. However, turnover tends to be high suggesting assets may be resold to New Zealanders in future (although New Zealanders may need to buy back a higher value).

Valuation changes

166 All else equal, an increase in demand will increase the value of assets.

167 While this increase in price creates the windfall for the current owners discussed above, it may affect affordability in the following ways:

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[9] See for example Greenaway and Kneller, 2007; Hayakawa et al, 2010; Sanderson 2004; Fabling et al. 2008; Fabling and Sanderson, 2011.

[10] Productivity spillovers from foreign direct investment in New Zealand, 2014, MBIE, https://www.mbie.govt.nz/dmsdocument/5776-productivity-spillovers-from-foreign-direct-investment-in-new-zealand

a. For productive assets, such as farms, the sales price will primarily be driven by factors affecting cash flow including global commodity prices (i.e. the price of milk), the productivity of the farm, and the quality of the land.

b. There is limited data to assess the impact of foreign demand on domestic property prices. Notwithstanding this, the government has opted to retain the ban on the sale of residential homes and lifestyle properties.

c. Luxury or trophy homes located outside of main centres, such as coastal properties or high-country farms, may increase in value. The sale of these homes to high-net worth individuals may also come with economic benefits such as increased relationship or investment in New Zealand.

Profits going abroad

168 A common criticism is that FDI will lead to profits going offshore. However, where markets are functioning well New Zealand will be paid a lump sum to compensate it for the net present value of future expected income.

Competition and firm closures

169 There are risks associated with anti-competitive practices, notably in industries that may enjoy a natural monopoly. These competition issues are not unique to foreign investment and are regulated by the Commerce Commission.

A deterioration of the current account

170 Changes in financial flows may be offset by changes in New Zealand's current account, although the impact is unclear as it will depend on the behavioural change with respect to savings and investment.

171 There are risks for the Government associated with an increase in external liabilities, including an increased in New Zealand's perceived riskiness that may lead to higher risk premium or change in the sovereign rating.

172 There is also a risk that sustained increase in the current account deficit may increase the risk of a future balance of payments crisis. Sound macro settings, including a floating exchange rate, moderate this risk. However, FDI is a relatively stable form of financing.

173 The longer-term implications for the current account are less clear as this will depend on how the proceeds from sales are reinvested. Investment in firms that increase productivity increase New Zealand's competitiveness. Higher productivity firms are more likely to export.

Additional risks

174 As noted, there is some possibility that a move to risk-based screening may increase the likelihood that investments will be consented without risk being detected. These implementation or operational risks will be considered through the design of operational processes and government policy to target risk.

Risks to international relationships

175 Although the regime is remaining country neutral, it is important that the design of the regulations and implementation occur in such a way that does not inadvertently create a perception that investors from some countries are treated differently to others. While some risk to international relationships can be managed, a move toward a "risk based" approach could be perceived as discriminatory if the basis for screening is not clear. Over time this uncertainty could hinder New Zealand's ability to attract investors from a small number of major markets for reputational reasons.

176 s6(a)

Other impacts

177 There are also a number of one-off implementation costs. In Treasury, these will be met by baseline funding. In LINZ, these will be met by the memorandum account and will likely be recovered from applicants.

Summary – marginal costs and benefits of the option

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	Some costs involved with developing an understanding of the new system.	Low – average compliance costs and application complexity should decline under fast-track consenting	Medium
Regulator – Land Information New Zealand (Overseas Investment Office)	One-off implementation costs to make necessary IT system changes and operational policy updates.	Low (<$3m)	Medium
Others (eg, wider govt, consumers, etc.)	The fast-track screening process may increase chances of some investments that pose risks to New Zealand's interests being consented without any scrutiny.	Low	Low
Additional benefits of the preferred option compared to taking no action			
Regulated groups	Streamlined fast-track consenting process will: - Reduce overall costs for applicants (compliance costs associated with uncertainty and delay) - Reduce consenting timeframes for the vast majority of applications. Increase certainty/predictability of the screening process, which will better support their investment decision-making.	Medium	Medium
Regulated parties:	Faster, more predicable consenting framework will help improve attractiveness of New Zealand assets and enable greater	Medium – cross-country evidence suggests reductions in screening restrictions can result in a	Low-medium

Vendors (New Zealand or overseas persons intending to sell an interest in New Zealand assets covered by the Act)	and quicker access to capital for New Zealand businesses.	meaningful increase in direct investment into firms each year.[11]	Evidence is reasonably robust but is based on the OECD restrictiveness index which has limitations (see discussion page 6)
	For businesses attracting foreign investment foreign investment, this could lead to: - Better access to new technologies and innovation - Better access to global markets - Increased productivity.	Low – quantitative analysis of productivity spillovers arising from FDI is non-conclusive.	Medium
	For employees of businesses attracting foreign investment, this could lead to: - Higher earnings - Increased opportunity to gain skills.	Moderate – Evidence shows 2-4% premium amongst similar workers	Medium
General	Attracting more foreign investment into New Zealand through streamlined screening regime will support economic growth through job creation, increased total output and productivity (and taxable profits).	Unclear – it is difficult to estimate the overall impact of investment flows as there are various factors other than the overseas investment regime that influence investors' decisions.	Mixed

[11] See for example: The Determinants of Foreign Direct Investment: Do Statutory Restrictions Matter? https://www.oecd.org/content/dam/oecd/en/publications/reports/2019/03/the-determinants-of-foreign-direct-investment_c371303e/641507ce-en.pdf

Section 3: Delivering an option

How will the new arrangements be implemented?

178 The proposed changes will require:

a) Changes to the way investors apply for consent, especially for transactions under the new National Interest pathway, to balance the regulator's need for information with the time and cost for the investor,

b) Significant changes to the way the regulator considers applications for consent, especially for transactions under the new National Interest pathway,

c) Changes to IT systems, including externally facing application forms and internal workflow systems,

d) Transitional arrangements for investors holding existing consents and standing consents and investors with applications which are being reviewed by the regulator upon commencement of the changes, and

e) Communication, education and engagement with the professionals and others who advise and engage with investors (including lawyers, accountants, immigration consultants, and government agencies).

179 An implementation plan will be developed by the regulator, with the support of Treasury, as the legislation progresses.

180 The Regulator will monitor compliance with these changes as it does for the Act more broadly and put in place a risk-based approach to encourage it. The regulator will encourage compliance by ensuring the system is easy for investors to navigate, providing education, and where necessary, taking enforcement action.

181 A summary of implementation risks and mitigations is outlined in the following table:

Risks	Mitigations
Resourcing	
Insufficient subject matter expertise to both implement the changes and continue to operate the existing rules effectively leads to delays	• Ensure implementation programme is appropriately resourced to recruit appropriate expertise. • LINZ will monitor the resourcing requirements to ensure workload and resource allocation are aligned.
Fundamental changes to the Act lead to difficulties processing applications submitted soon after commencement	• IT systems are redeveloped to be fit for purpose, easy to use, adaptable, and automate as many processes as possible. • Where possible, LINZ will consider implementing new processes progressively between now and commencement.
Limited time to implement the changes	• Implementation planning will be refined as each tranche of policy decisions is made. • LINZ will finalise the implementation plan once decisions are made on a likely commencement date.

It is difficult to forecast the impact of the changes on application numbers leading to inaccurate resourcing estimates	• Have additional resources identified and ready for redeployment should volumes be significantly greater than expected.
Stakeholder engagement	
Significant changes to the regime create uncertainty for investors and lawyers	• A communication plan is developed including education materials to support the reform and proactive engagement is undertaken. • LINZ has regular engagement with a legal reference group and uses existing communication methods, including monthly newsletters and webinars, to share messages about the reforms.
Expectations and direction	
LINZ has insufficient clarity of the risks that Government wishes to receive greater scrutiny.	• Treasury will support a process to identify risks and populate the GPS in a manner that provides clarity for the regulator.
The changing nature of investment may highlight unanticipated risk which leads to delays in assessment.	• Clear GPS guidance can be provided on how to approach novel investments.

How will the new arrangements be monitored, evaluated, and reviewed?

182 The regulator collects data on consent applications, notifications under the NSPO regime, compliance with conditions of consent, and non-compliance with the Act generally. This will help to inform an assessment of the success of the new regime.

183 Treasury will work closely with LINZ to identify issues with the new regime, changes in the risk environment, and potential responses. Treasury will utilise existing institutions established to meet its regulatory stewardship function for the regime for this purpose. These include the standing committee on investment, which is a cross-agency group that considers foreign investment risk.