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What changes to expect in New Zealand's overseas investment laws next month

and why New Zealand remains open for business

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As recently announced by the Government, certain amendments to the Overseas Investment Act 2005 ('**Act**') will be fast-tracked into law in response to COVID-19. A number of significant changes were already proposed for the Act before New Zealand went into 'lockdown' in late March – but now, some of these initiatives, including a particular 'urgent' measure, will be implemented ahead of schedule.

The key policy balance that the Government is seeking to strike is the protection of vulnerable firms and assets from 'fire sales' to overseas interests, whilst not jeopardising the viability of financially distressed businesses. Overall, we are not surprised by the Government's responses to overseas investment, given similar approaches taken in other jurisdictions such as Australia and Canada.

Introduction of a temporary notification regime

Certain changes to the Act will be expedited under the Overseas Investment (Urgent Measures) Amendment Bill through a truncated Select Committee process in June 2020. Other changes to the Act will be progressed under a separate bill, the Overseas Investment Amendment Bill (No 3), over a longer time period.

In our view, the most significant of these is the introduction of a new temporary notification regime.

Under this new regime, overseas investment transactions that are not already subject to screening under the Act will need to be notified to the Overseas Investment Office ('**OIO**'), where the transaction involves:

- an acquisition of more than 25% ownership or control interest in a New Zealand business;
- an increase in the overseas person's existing 25% or more ownership or control interest in a New Zealand business to (or more than) 50%, 75%, or 100%; or
- the acquisition of assets used in carrying on business in New Zealand that effectively amounts to a change in control of the business.

The notification obligation will apply regardless of the dollar value of the transaction or whether any interest in land is involved.

Once notified, the Minister will assess the transaction against a 'national interest' test, and the transaction cannot be effected unless a direction order is made. The Government will have wide-ranging 'call-in' powers in relation to the notified transactions, including permitting the transaction (with or without conditions), prohibiting the transaction, ordering disposal of the investment considered contrary to the national interest, or even placing the relevant business under statutory management.

The temporary notification requirement is not intended to be a process that delays legitimate investments. Investors should expect to hear within 10 days whether a notified transaction could be contrary to New Zealand's national interest. Those transactions that would not be contrary to our national interest would be able to proceed quickly, although the transactions that pose a risk to our national interest will become subject to a more detailed assessment (which could take between 40 and 70 days to process).

These timeframes assume that the OIO will be in possession of all relevant information from the investor, so the actual timeframe for processing a notified transaction could be even longer if it could pose a risk to our national interest.

Whilst we expect that giving notification, in itself, will be a straightforward exercise, the uncertainty in the timeframe for processing a notified transaction (not to mention the risk of the transaction being altered or blocked) could be perceived as a material obstacle for an overseas investor. To avoid unnecessary delays and surprises, we would encourage investors to obtain legal advice and notify the OIO as soon as a transaction opportunity has been identified.

What is the 'national interest' test?

The 'national interest' test is similar to the test that underpins the Australian foreign investment regime, and will serve as a 'backstop' tool to manage significant risks associated with transactions already screened under the Act. The introduction of this test into the Act was contemplated well before COVID-19.

Essentially, under this test, the Government will be able to decline consent to an overseas investment transaction that it regards as contrary to New Zealand's national interest. Such transactions will be those that already require consent under the Act and would result in:

- an investment in 'strategically important businesses' (or '**SIBs**') – such as businesses in military or dual-use technology, ports or airports, electricity, water, telecommunications, media businesses with significant impact and financial market infrastructure, and critical direct suppliers to intelligence or security agencies;
- an investment where a non-New Zealand government investor has 10% or more ownership or control interest in the investor; or
- other investments which have been identified to pose material risks to New Zealand's national interest.

How long would the temporary notification regime last for?

The notification regime described above is temporary, and will operate while the COVID-19 pandemic and its associated economic effects continue to have a significant impact in New Zealand. The regime will also be reviewed every 90 days.

When COVID-19 is over, the notification regime will be replaced by a permanent 'call-in power', which will only apply to overseas investment in SIBs.

Other changes to make the OIO process better

As part of the expedited changes to the Act, a series of other positive amendments designed at simplifying the screening process for overseas investment will be made. The incumbent consenting process under the Act has long been criticised by overseas investors as being an arduous exercise, characterised by undue administrative complexities, uncertainty as to timing and delay. These other amendments will improve predictability and reduce the associated administrative complications.

Investor Test

The current consent regime under the Act requires an overseas investor to satisfy a number of criteria collectively known as the 'Investor Test'.

Under the proposed changes, the current criteria relating to 'business experience and acumen' and 'financial commitment' will be removed when assessing an investor's character and capability. Further, only serious and proven matters and allegations will be considered for the test.

In addition, overseas persons who have already passed the Investor Test will not need to re-satisfy the test in full each time they subsequently propose to make another investment. Investors will be able to apply at any time for an assessment of whether they meet the test (and not just when they apply for consent for a particular investment).

Low-risk transactions

Some low-risk investments which currently require consent under the Act will become exempt. For

example, a New Zealand-incorporated company whose financial products are quoted on the NZX Main Board will no longer be an overseas person for the purposes of the Act, unless:

- the company is more than 50% beneficially owned by one or more overseas persons; or
- one or more overseas persons who each own 10% or more of the financial products, either:
    - individually or together control the composition of 50% or more of the company's board of directors; or
    - exercise or control the exercise of more than 25% of the voting power at a meeting of the company's shareholders.

Other changes

Other notable improvements include increasing the screening threshold for leases and other less-than-freehold interests from 3 years to 10 years (which is relevant for 'sensitive land' assessments under the Act), and reducing the scope of 'adjoining land'.

Statutory timeframes for decisions by the OIO and Ministers will also be introduced, although the purpose of imposing such timeframes is to motivate, rather than compel, compliance by these decision-makers.

Other exemptions will also be introduced under the regulations, to support New Zealand businesses' ability to access debt and equity financing from overseas sources.

What will the changes actually mean?

The status quo will continue for overseas investment transactions that are currently within the ambit of the Act, between now and the implementation of the Overseas Investment (Urgent Measures) Amendment Bill and the Overseas Investment Amendment Bill (No 3). The former is expected to become law during June 2020, and will be supported by regulations to be drafted.

Once the Bills are passed and the amendments enacted, the landscape for overseas investment transactions will look significantly different. However, our assessment is that other than the administrative burden for overseas investors on notifying the OIO of their intention to invest (which is a temporary measure), not much will change, and in fact, the permanent changes that take place will ultimately be positive. Early engagement of legal advice will help to mitigate the risk of delays in investment timeframes, and provide more comfort regarding the viability of the transaction.

We do not expect the Government to exercise its 'call in' powers lightly, to alter or block commercially negotiated transactions, except in exceptional circumstances. This is especially the case where the ultimate commercial outcome of government intervention is the failure of a business, that the Government has no mandate to underwrite. New Zealand remains a country that needs the assistance of foreign capital to recover economically from COVID-19, and there is no policy justification for creating more uncertainty for overseas investors when the Government seeks to simplify the screening process for overseas investments.

Of course, a robust screening process for predatory acquisitions involving struggling businesses operating in commercially and politically sensitive sectors is warranted – but transactions of that nature or size would likely have triggered a consent requirement under the existing Act and regulations anyway, especially in an election year when there is greater risk of foreign investment matters becoming political, rather than commercial, issues.

We intend to publish a summary of other changes to the Act as part of the 'Phase Two' reforms to the Act in the next 12 months, through a subsequent publication. In the meantime, we would like to emphasise that the recently announced changes do not represent an overseas investment freeze. New Zealand very much remains open for business and investment, and needs foreign capital to rebuild more than ever.

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