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A future for Foreign Direct Investment into New Zealand

Introduction

BusinessNZ has long advocated for a more open and welcoming Foreign Direct Investment (FDI) regime, and it is clear that there remains an appetite for this stance within business circles. At the same time, the new coalition government appears to be open to a more permissive approach. The concern is that the regime governing FDI is too restrictive, and that the country has not enjoyed the full range of benefits that FDI can bring.

This paper considers the case for change in the framework for managing FDI, and it specifies which broad aspects of the framework most need to be changed. It also identifies which need to be kept unchanged.

What is FDI?

FDI involves an investment made by a company, individual, or government from one country into a business or project in another country. It can involve the simple acquisition of an existing asset in the host country without further development: for example, a piece of real estate. Perhaps more commonly, it involves the acquisition of an existing business enterprise, or the creation of an entirely new enterprise. In the case of the acquisition of an existing business enterprise, there may or may not follow further development of the business.

Why FDI is important

Foreign Direct Investment (FDI) can provide a number of benefits to the host economy. These include:

- Stimulus to the national economy when the investor employs people, participates in supply chains, exports and pays taxes.
- Enhancement of workforce capacity and capability through training and improved management practices.
- Access to technology and skills transfer through engagement in international corporate networks.
- Increased levels of Research and Development.
- Improved capital inflows.
- Deepening of international relations.

These things will generally increase productivity levels and help to improve living standards.

The benefits can apply both to FDI that involves acquisition of existing businesses, and to the creation of businesses that are entirely new. They apply less to FDI that simply involves the acquisition of real estate that is not further developed.

Is there a downside to FDI?

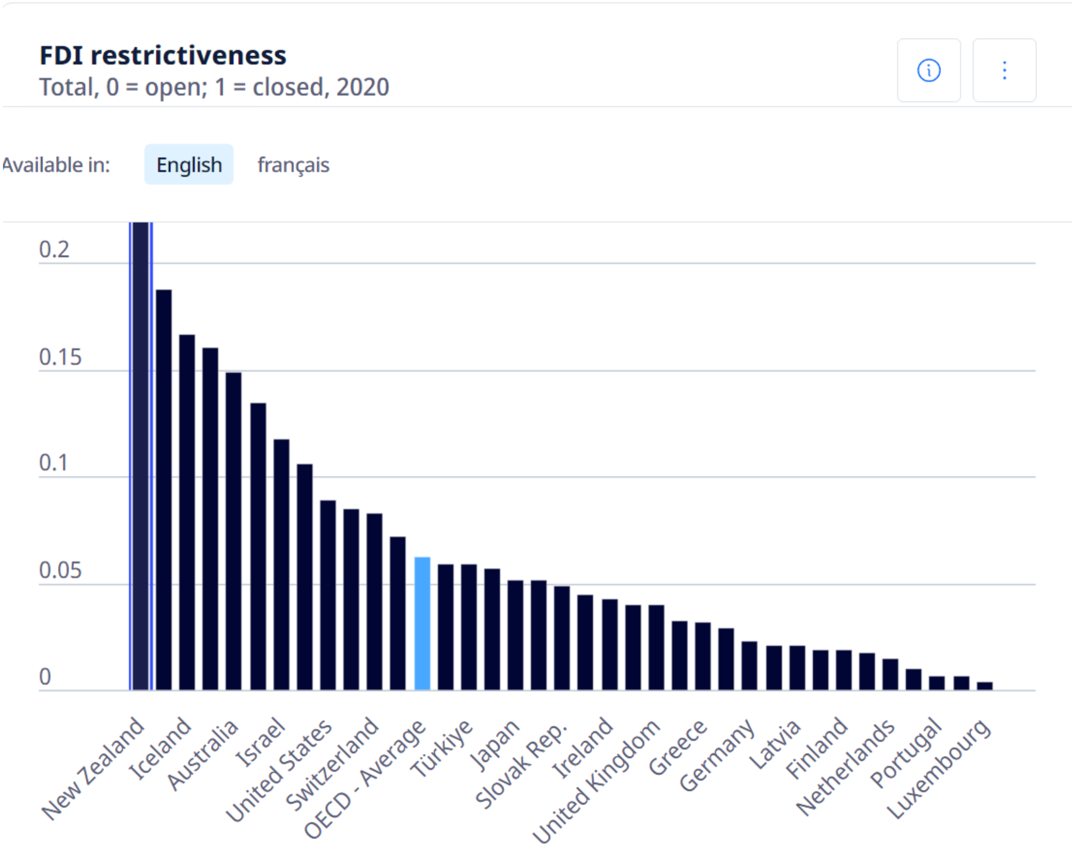
It should be recognised that FDI is not automatically wholly beneficial to the host country. Actual or potential disbenefits include:

- Increased competition between businesses leading to a shortage of capital or labour ("crowding out").
- Repatriation of profits to the investor's home country.
- Loss of economic sovereignty and dependence on foreign powers.
- Environmental or cultural harms.

On balance, however, most developed economies perceive the benefits of FDI to outweigh the downsides, and this is why most regard it positively, even though many control it to a greater or lesser extent.

How does New Zealand rank in terms of restrictions on FDI?

According to the OECD,[1] New Zealand has the most restrictive FDI regime of all countries that belong to the organisation. Moreover, the screenshot below indicates that the degree of restrictiveness in NZ is not only greater than the average for the OECD, but that it is very much greater.



[1] https://www.oecd.org/en/data/indicators/fdi-restrictiveness.html

Exactly how FDI restrictiveness should be measured might be open to debate, but it should be noted that the OECD uses an index gauging the restrictiveness of a country's FDI rules. The index takes into account four main types of restrictions: foreign equity restrictions; discriminatory screening or approval mechanisms; restrictions on key foreign personnel and operational restrictions.

Problems with New Zealand's FDI framework

In BusinessNZ's opinion, the statement in the Overseas Investment Act 2005 that "*The purpose of this Act is to acknowledge that it is a privilege for overseas persons to own or control sensitive New Zealand assets …*" sends an unnecessarily negative message to potential investors.

The lack of welcome is reinforced by the fact that the Overseas Investment Office (OIO) is part of Land Information New Zealand (LINZ) and doesn't even have its own website. In addition, the OIO pages on the LINZ website focus almost exclusively on the rules and are graphically unattractive.

Overall, New Zealand's message to potential investors could be expressed as saying: "*Prove that you are worthy of the privilege of being an investor in NZ*." This is in stark contrast to the website of Ireland's Foreign Direct Investment agency, IDA Ireland[2], which could be summarised as saying: "*Welcome. How can we help you*?"

A meeting on 2 August 2024, between BusinessNZ members and Treasury officials, indicated that there was a desire, at least from business, for changes, if not a radical reform of the legal framework and the administrative control, starting with first principles review.

In summary, the key arguments from business were:

- OIO processes are complex, opaque and slow
- Potential investors are not given any clarity on the likely outcomes of the process
- There needs to be more recognition of the benefits of FDI and what overseas investors/parent companies bring.
- It needs to be clear that overseas investors have choices about where they invest.
- It is too hard at the moment for overseas companies to invest in NZ – NZ's offering is relatively unattractive.
- There needs to be a "trusted investor" category, or similar, for long-established overseas investors that want to invest further.
- Resource consents should have a longer lifetime, 20+ years instead of 5-10
- The National Interest test is far too frequently triggered as a result of non-NZ government investors being involved in an investor's structure.
- Barriers to purchase of assets by overseas investors can have widespread negative consequences in the economy, especially where there are no NZ buyers for assets for sale.
- The definition of Sensitive Land is too broad.

Comments from the business people at the meeting included:

> *"From a private equity perspective it's a black box: no transparency, no certainty of process. Are we benchmarking around the world? We must have foreign capital in technology or we just can't scale."*

[2] Ireland's Foreign Direct Investment Agency | IDA Ireland | IDA Ireland

"(Law Firm) – *It costs in time and money. Clients say if they knew how hard it was going to be, they wouldn't have applied."*

"There is no certainty of time or cost, at the moment it's a roll of the dice."

"There is no recognition of longevity of long-term investment and ownership. If you want to expand you are treated as starting from scratch."

"Investors need access to resource consents for 20-30 years, 5-10 years is not long enough!"

"A healthcare provider with a residential offering has to get another approval for 3 years, do Kiwis really care about that?"

"With the sensitive land test, investors are worried they can not exit the investment if they haven't delivered the benefits required."

What the coalition government has promised to do in relation to FDI

National's Coalition Agreement with NZ First and its Agreement with ACT both state that the National Party's Fiscal Plan, Tax Plan, 100-day plan and 100-point economic plan will apply, except for the specific exemptions which have been agreed between the Parties and set out in the respective Coalition Agreement documents.

The only matter in the National – NZ First agreement that is relevant to FDI is:

"*Tax relief will be progressed as set out in National's Tax Plan, but will not include a repeal of the foreign buyer's residential property ban, with income tax reductions coming into force from I July 2024"*[3]

The only matter in the National – ACT agreement that touches on FDI is:

"*Amend the Overseas Investment Act 2005 to limit ministerial decision making to national security concerns and make such decision making more timely."*

By implication, the coalition agreed to the following in National's 100 Point Plan to Rebuild the Economy:

"*Ban foreign farm-to-forest conversions for carbon farming."*

And

"*Amend the Overseas Investment Act and Income Tax Act to give investors certainty to invest in Build-to-Rent projects."*

It appears, therefore, that the coalition would be open to significant changes to New Zealand's FDI regime.

What, specifically, needs to be done?

The problems identified by businesses and the other information summarised above, imply there is a case for significant reform of the law governing FDI into New Zealand. We also believe the administration of the rules and processes related to FDI should be changed.

[3] This matter has already been acted on.

Concerning the law, the Overseas Investment Act should be reviewed, starting with consideration of how the Purpose Statement should be changed to establish a positive message about how New Zealand regards overseas investors. The specific provisions of a reformed Act would reflect this, with the overall aim of creating a framework that welcomes and facilitates FDI.

Nonetheless, we believe that some restrictions on FDI would need to remain. We recognise that some types of foreign investments could be harmful. We also recognise that investments by some foreign entities could harm New Zealand's standing in the international community. Accordingly, a reformed Overseas Investment Act should be designed to enable actual and potential harms to be prevented.

Regarding the administration of the rules and processes related to FDI, it is difficult to understand why the OIO is merely an adjunct to LINZ. We believe that the OIO should become a stand-alone government agency, with its own strategy. A new, stand-alone Overseas Investment Agency would also need its own website, especially one that conveys more positive and welcoming messages.

A starting point for the establishment of a stand-alone Overseas Investment Aency should be an examination of how other countries market themselves as hosts for FDI, to learn lessons that could be applied in New Zealand. Ireland was cited above as an example of better marketing, but there may well be other examples to learn from.

Going beyond changing the Overseas Investment Act and the Overseas Investment Office, there is also a case for revising taxation rules that apply to high-net-worth individuals, so as to encourage them to migrate to New Zealand, or to make it more favourable for them to stay. As pointed out by the NZIER[4], New Zealand is not attracting enough talented people because of the country's international tax policy settings. While New Zealand's migration settings are welcoming, the tax settings require newly arrived migrants, and some returning Kiwis, to pay tax on offshore investments they made before coming here. Moreover, they are often required to pay annual tax on the paper value of investments that do not provide any cash return and may never actually do so.

Conclusions

This note has shown that New Zealand is very restrictive, compared to other countries, when it comes to FDI. It has also highlighted problems, both in terms of the tone of the current Overseas Investment Act, and with the operation of the Overseas Investment Office. These shortcomings need to be rectified.

BusinessNZ believes that the benefits of FDI to New Zealand are great, and that there is an opportunity create the conditions for attracting more FDI into the country. There are potential harms, but we believe they are less than the benefits, and also that they can be managed.

We are encouraged that the coalition agreement between National and ACT specifies a policy that the 2005 Overseas Investment Act should be amended to limit ministerial decision making to national security concerns. However, the question is whether there should be a first principles review of the existing legislation, leading an entirely new Act, or an amended Act that focuses on the low-hanging fruit.

We look forward to progress being made to signal to the world that New Zealand positively welcomes FDI.

[4] The place where talent does not want to live - The intersection of New Zealand immigration and tax policies in a globalising world (NZIER April 2024)

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