New Zealand Superannuation and Retirement Income (Controlling Interests) Amendment Bill

227—1

Report of the Finance and Expenditure Committee

August 2023

Contents

Ingrid Leary
Chairperson

New Zealand Superannuation and Retirement Income (Controlling Interests) Amendment Bill

Recommendation

The Finance and Expenditure Committee has examined the New Zealand Superannuation and Retirement Income (Controlling Interests) Amendment Bill and recommends to the House that it be passed without amendment.

About the bill

The New Zealand Superannuation and Retirement Income (Controlling Interests) Amendment Bill would amend the New Zealand Superannuation and Retirement Income Act 2001. That Act created the New Zealand Superannuation Fund (NZSF), a sovereign wealth fund, to help cover the cost of superannuation for future generations. The Act also established the Guardians of New Zealand Superannuation, a Crown entity, to manage the NZSF and its investments.

At present, section 59 of the Act requires the Guardians to use their best endeavours to ensure that the NZSF does not take a controlling stake in an entity.[1] The bill would repeal and replace sections 59 to 59B to remove this restriction.

Removing the restriction would represent an important new power for the Guardians. To balance this power, the bill would add to existing controls in the Act by also amending:

- section 61, to require the Guardians' statement of investment policies, standards, and procedures to include details of the governance framework for the implementation and operation of controlled entities
- Schedule 1AA of the Act, to require that the first or second periodic performance review (provided for in section 71) after the amendment took effect include a review of the operation and effectiveness of the amendments made by the bill.

Finally, the bill would make minor related and consequential amendments to:

- the Ombudsmen Act 1975 and the Official Information Act 1982, to apply them to the Guardians and its Crown entity subsidiaries, but not to any other private sector subsidiaries that the Guardians might acquire should the bill be passed
- the Income Tax Act 2007, to address the removal of references to fund investment vehicles, and to preserve the current tax treatment of NZSF investments.

1 Section 59A provides an exception to this restriction, for fund investment vehicles. We discuss these vehicles later in our report.

The bill results from a review of the restriction in section 59 by the Treasury in 2021.[2] This review followed a 2011 review that led to the insertion in 2015 of section 59A, which allows the NZSF to form, invest in, and control fund investment vehicles.

Legislative scrutiny

As part of our consideration of the bill, we have examined its consistency with principles of legislative quality. We have no issues regarding the legislation's design to bring to the attention of the House.

Submissions received on the bill

We received seven submissions on the bill from a mix of organisations and individuals. Four submitters gave full or qualified support for the bill, while two were opposed and one offered no opinion. Some submissions referred to issues that we consider to be outside the policy intent of the bill.

We do not recommend any changes to the bill as introduced on the basis of the submissions we received. Nevertheless, some submissions relate to key issues that we think merit further discussion. We discuss these issues below.

Key issues that we considered

We sought advice from the Treasury and our independent adviser on four key issues that arose in considering this bill.

Benefits and risks of removing the restriction on controlling interests

We understand that the main benefit of removing the restriction on controlling interests would be to allow the Guardians to invest directly in a wider range of investment opportunities in New Zealand, where such opportunities are relatively few. It would give the Guardians more flexibility when entering and exiting a holding, providing additional capital to investee entities, or influencing board and shareholder decisions on, for instance, ESG matters (environmental, social, and corporate governance). Removing the restriction would also enable the Guardians to use simpler ownership structures, and take fuller advantage of investment opportunities.

On the other hand, one potential risk of this change is that it might compromise the Guardians' independence from public or ministerial pressure. For example, allowing the NZSF to take controlling stakes might lead to pressure to bail out distressed New Zealand companies. We understand that this risk was considered when the Act was first developed, and the following protections were included to mitigate it:

- Section 58(2) of the Act requires the Guardians to invest the fund on a prudent, commercial basis. The Board of the Guardians is responsible for the Fund's

[2] The review is available on the Treasury's website.

performance, and for ensuring that the Fund invests in a commercial manner irrespective of ministerial or public pressure.

- Section 64(1) and (2) of the Act provide that the Minister can give only non-binding directions to the Guardians regarding the Government's expectations of the Fund's performance, including as to risk and return. Further, the Guardian's board is appointed at "arm's length" from the Minister, via nominations from a separate nominating committee, with each board member required to have substantial expertise in the management of financial assets.

The bill's proposed amendments to section 61 and Schedule 1AA of the Act aim to supplement these existing protections.

Constraining the Guardians' investment mandate in legislation

One alternative that we considered to the approach in the bill, particularly the proposed amendments to section 61, was to enact in primary or secondary legislation further constraints on the NZSF's approach to investments where it has a controlling interest. On balance, however, we consider that this would run counter to the existing structure of the legislation, which empowers the Guardians to act independently, including by developing best-practice rules and policies for investment.

In this regard, we note the positive findings of the 2019 statutory independent review of the Guardians by Willis Towers Watson. Those findings commented favourably on the Guardians' governance model, and on the Guardians' approach to considering domestic assets for investment.[3]

Guardians' capacity to use controlling interests effectively and responsibly

We were interested in what skills and capabilities the Guardians would need in order to exercise the power proposed in the bill effectively and responsibly.

We note that businesses in which the NZSF held a controlling interest would remain operationally independent, standalone entities. The boards of directors of those entities would be chiefly responsible for their governance. The Guardians' role and rights would be limited to those of investor or shareholder. Therefore, the Guardians would not need to acquire new corporate management expertise.

The Guardians' own board would specify the governance and risk mitigation controls on the acquisition and management of interests in controlled entities, through its statement of investment policies, standards, and procedures. The statement is already required of the Guardians' board, so this would not entail additional expertise.

[3] A copy of the 2019 independent review by Willis Towers Watson is available on the New Zealand Superannuation Fund's website.

Guardians’ present use of fund investment vehicles to take controlling interests

We were interested in the Guardians’ use currently of what are known as “fund investment vehicles” (FIVs) to take controlling interests. We note that the NZSF has in fact been able, since its inception, to acquire controlling interests in assets, such as rural land and real estate. However, it has not been able to take a controlling interest in more active operating companies.

Since the Act was amended in 2015, the NZSF has also been able to hold controlling interests in FIVs. FIVs are entities formed or controlled for the purpose of holding, facilitating, or managing the NZSF’s investments (including investments in assets). As a result, the Guardians gained the ability to hold assets, such as rural land, in FIVs, and to control these FIVs.

However, we note that the restriction on controlling interests continued to apply to any entities held by FIVs. In addition, the Guardians’ statement of investment policies, standards, and procedures recognised that FIVs cannot be used to circumvent the restriction on holding controlling interests in active operating companies. The bill would allow them to do so, and would therefore represent a meaningful change to what the Guardians could do.

Concluding comments

We thank submitters for their submissions. We acknowledge that some submitters opposed the bill. However, we are persuaded that the bill could yield real benefits for both the NZSF and the New Zealand economy.

In addition, we think the proposed inclusion of requirements for the governance of controlled entities in the Guardians’ own primary investment documents should operate as a sufficiently flexible, yet binding, set of rules to help mitigate the risks of taking controlling interests. The bill’s inclusion of a five-yearly review of how the changes are operating would also be an opportunity to check whether this was the case in practice.

Appendix

Committee procedure

The New Zealand Superannuation and Retirement Income (Controlling Interests) Amendment Bill was referred to the committee on 9 March 2023. The closing date for submissions was 24 April 2023. We received and considered submissions from seven interested groups and individuals. We did not hear any oral evidence.

We received advice on the bill from the Treasury and our independent adviser, Jeremy Muir. The Office of the Clerk provided advice on the bill's legislative quality. The Parliamentary Counsel Office was available to assist with legal drafting.

Committee members

Ingrid Leary (Chairperson from 17 April 2023)
Hon Rachel Brooking (Chairperson until 12 April 2023 and member until 3 May 2023)
Andrew Bayly
Hon Dr David Clark
Shanan Halbert (until 3 May 2023)
Anna Lorck
Dan Rosewarne (from 3 May 2023)
Damien Smith
Chlöe Swarbrick
Hon Phil Twyford
Simon Watts
Helen White (until 8 February and from 3 May 2023)
Nicola Willis

Advice and evidence received

The documents that we received as advice and evidence are available on the Parliament website, www.parliament.nz.