

# Departmental Disclosure Statement

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Venture Capital Fund Bill
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The departmental disclosure statement for a government Bill seeks to bring together in one place a range of information to support and enhance the Parliamentary and public scrutiny of that Bill.

It identifies:

- the general policy intent of the Bill and other background policy material;
- some of the key quality assurance products and processes used to develop and test the content of the Bill;
- the presence of certain significant powers or features in the Bill that might be of particular Parliamentary or public interest and warrant an explanation.

This disclosure statement was prepared by the Treasury and the Ministry of Business, Innovation and Employment.

The Treasury and the Ministry of Business, Innovation and Employment certify that, to the best of their knowledge and understanding, the information provided is complete and accurate at the date of finalisation below.

22 August 2019

## Contents

Part One: General Policy Statement.....	3
Part Two: Background Material and Policy Information .....	6
Part Three: Testing of Legislative Content.....	8
Part Four: Significant Legislative Features .....	10

## Part One: General Policy Statement

### Introduction

This Bill—

- establishes a Venture Capital Fund (the **VCF**); and
- provides for the Guardians of New Zealand Superannuation (the **Guardians**) to manage and administer the VCF.

### Early-stage capital markets in New Zealand

Well-functioning early-stage capital markets are required to support investment in new internationally competitive firms and capabilities. This in turn will support New Zealand to shift to a more productive, sustainable, and inclusive economy.

Government interventions have had limited success to date in developing a well-functioning early-stage domestic venture capital industry, particularly in the Series A and B funding stages.

Many early-stage high-growth companies continue to struggle to access the capital they need to develop to their potential. This leads them to being either constrained in their growth or having to seek foreign investment to overcome this funding gap, and may require start-ups to sell down prematurely or move abroad. This may also result in the shareholder value of any success accruing to offshore investors rather than being recycled back to domestic investors and the domestic venture capital ecosystem. This limits the economic benefits to New Zealand from its research and development and science investments.

This Bill establishes a Venture Capital Fund with the purpose of contributing to a sustainable and productive economy by—

- increasing the venture capital available to New Zealand's entities; and
- developing New Zealand's venture capital markets to function more effectively so that over time—
  - more venture capital is available to New Zealand entities from sources other than the VCF; and
  - New Zealand entities that receive venture capital are more likely to grow into successful and sustainable businesses.

Institutional investors exert control over a significant amount of capital, and provide signals to smaller New Zealand or overseas investors on where to invest. However, New Zealand's institutional investors have not yet invested in domestic venture capital markets to a material extent. More developed venture capital markets, with better resourced and connected fund managers that generate returns appropriate for the sector, should help attract private capital and new investors into this sector. These may include domestic institutions, KiwiSaver fund managers, corporates, iwi, private family investments, retail investors, and some offshore investors.

The Guardians will manage and administer the VCF, utilising best-practice investment management that is appropriate for institutional investments in New Zealand's venture capital markets (subject to high-level Government policy requirements). The Bill proposes that the Guardians (itself or through a VCF investment entity, such as a limited partnership) will enter into a contract or other arrangement with New Zealand Venture Investment Fund Limited (**NZVIF**), whereby NZVIF will invest the VCF capital using a "fund of funds" model on establishment.

The benefit of requiring the Guardians to manage and administer the VCF is to leverage its existing frameworks and expertise to apply best-practice investment management oversight of NZVIF as the initial designated manager of the VCF. In turn, the intent is that NZVIF will facilitate best practice with underlying venture capital fund managers.

The fund of funds model will make investments into or alongside privately managed venture capital (**VC**) funds. The role of the fund of funds manager is to select private funds that meet the requisite criteria for investment.

The benefits of NZVIF being the initial investment manager are that the VCF will benefit from NZVIF's existing market relationships, its experience of operating in the early-stage capital markets, and its expertise and experience from managing a domestic venture capital fund of funds programme since 2002.

The private VC funds will make decisions on which companies to support, how to support them, and when to stop supporting them. The private VC funds will be required to, among other criteria, prove their capability and that they are able to raise a certain minimum amount of private capital before receiving investment from the VCF. The expectation is that a self-sustaining domestic venture capital market with sufficient capacity to service demand will develop as a result.

### **Why Bill is required**

A Bill is required as the Guardians is an autonomous Crown entity, established under the New Zealand Superannuation and Retirement Income Act 2001 (the **NZSRI Act**) to manage and administer the New Zealand Superannuation Fund (the **NZSF**). Under the NZSRI Act, the Guardians have no authority to administer and manage the VCF.

### **Amendments to New Zealand Superannuation and Retirement Income Act 2001**

To ensure that the Guardians can administer the VCF, this Bill amends the NZSRI Act to widen the Guardians' responsibilities to include administering the VCF. This is in addition to, but separate from, the Guardians' role in managing and administering the NZSF.

The proposed amendments make no changes to—

- the functioning of New Zealand superannuation
- the New Zealand Superannuation Fund
- the Guardians' role and responsibilities in managing and administering the New Zealand Superannuation Fund.

### **Venture Capital Fund Bill**

*Part 2* of this Bill will become the Venture Capital Fund Act. Rather than amend the NZSRI Act to include clauses to establish the VCF, it is more appropriate to bring into force a new Act for this specific purpose. The NZSF and VCF are separate funds, with separate mandates. There are no changes to the Guardians' mandate as regards the NZSF.

However, the NZSRI Act provides a useful starting point for the new Venture Capital Fund Act. One of the key similarities is that the Bill establishes the VCF as a standalone fund that is the property of the Crown.

The Bill requires the Guardians to invest the VCF in accordance with best-practice investment management that is appropriate for institutional investment in New Zealand venture capital markets. This duty is subject to requirements to—

- ensure that a substantial proportion of the VCF's capital will be made available to New Zealand entities through venture capital funds with a New Zealand connection. However, a proportion of the capital may go to foreign entities, or to foreign funds that have some connection to New Zealand, where this would support the market development objective (for example by adding to the expertise of local funds through overseas connections); and
- comply with, or have regard to, directions given by the Minister via a policy statement; and
- invest the VCF in a way that avoids prejudice to New Zealand's reputation as a responsible member of the world community; and
- enter into an arrangement with NZVIF to allow NZVIF to undertake investment of the VCF via a fund of funds model.

The policy statement will guide the core parameters and settings under which the Guardians and NZVIF will operate. These parameters and settings determined by the Minister will directly influence the VCF's investment performance.

The policy statement can also contain a range of items that the Guardians must, in managing and administering the VCF, have regard to, including the Government's—

- expectation as to when venture capital will be made available to New Zealand entities through the VCF; and
- expectation as to when the capital invested through the VCF will be returned to the Crown; and
- specified economic policy.

The policy statement also allows Ministers and the Guardians to include, by mutual agreement, other settings to the overall investment approach. This provides the flexibility to adjust the overall investment approach, while balancing the need for the Guardians to be accountable for managing and administering the VCF consistent with the overall investment approach. Additional settings and parameters might include the proportion of capital that can be committed to funds and firms outside New Zealand, the minimum size of a qualifying private fund, or how returns are shared and paid out.

Any changes to the policy statement will not affect any existing investments, matters, commitments, or contracts at the time the policy is amended.

#### **Guardians may apportion obligations (including expenses)**

The Bill allows the Guardians to apportion obligations (including expenses) between the NZSF and the VCF in a manner they consider reasonable, if they consider that an obligation is related to both the NZSF and the VCF. The expectation is that the way expenses and obligations are addressed as between the NZSF and appropriations will remain the same (and that a substantially similar approach will be applied for the VCF as well).

#### **Requirement for Guardians to use NZVIF**

The Bill requires that the Guardians and NZVIF make reasonable efforts to reach an arrangement. If no arrangement can be concluded, the Minister can specify the terms of an arrangement between NZVIF and the Guardians. This approach reflects the intention to draw on the respective expertise of the Guardians and NZVIF. However, the Guardians retain the right to cancel the arrangement in accordance with the terms of the arrangement between the Guardians and NZVIF.

#### **Winding up**

The Bill establishes a process by which the Minister may give a direction so that all or part of the VCF can be wound up and returned to a Crown Bank Account.

#### **Bill to be divided into 2 separate Bills**

It is intended that this Bill be divided into the following 2 separate Bills at the committee of the whole House stage:

- a New Zealand Superannuation and Retirement Income Amendment Bill
- a Venture Capital Fund Bill.

## Part Two: Background Material and Policy Information

### Published reviews or evaluations

<b>2.1. Are there any publicly available inquiry, review or evaluation reports that have informed, or are relevant to, the policy to be given effect by this Bill?</b>	<b>NO</b>
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### Relevant international treaties

<b>2.2. Does this Bill seek to give effect to New Zealand action in relation to an international treaty?</b>	<b>NO</b>
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### Regulatory impact analysis

<b>2.3. Were any regulatory impact statements provided to inform the policy decisions that led to this Bill?</b>	<b>NO</b>
<p>No. The absence of a regulatory impact assessment triggered Cabinet's requirement for a supplementary analysis report (CO (17) 3), including the preparation of a briefing by the Regulatory Quality Team (RQT). The RQT provided the following briefing:</p> <p>There are two main risks with not having a regulatory impact assessment. The first is that officials' analysis is inadequate – a risk to the quality of the proposal and for unintended consequences. The second is that Ministers, and then Select Committee, Parliament and the public, do not have complete information on which to make decisions – a transparency risk as well as a risk to the quality of the proposal.</p> <p>The RQT has considered the particulars of the current situation, including that the legislative change elements are a relatively small part of the overall proposal, and considers that the following approaches might be appropriate:</p> <ul style="list-style-type: none"><li>• The risk to the quality of the proposal could be partially addressed by a post-implementation review. The RQT notes that Cabinet has already agreed to a review at five years, so no additional decisions or work is required here.</li><li>• The risk to transparency could be addressed by proactively releasing the Cabinet paper and any significant internal background material prepared by MBIE and the Treasury prior to legislation being tabled. The material to be released could be agreed between RQT, Treasury and MBIE in consultation with Ministers.</li></ul>	

### Extent of impact analysis available

<b>2.4. Has further impact analysis become available for any aspects of the policy to be given effect by this Bill?</b>	<b>YES</b>
<p>Ministers have agreed to release the Cabinet papers and supporting analyses. This material will be available on the Ministry of Business, Innovation and Employment website.</p>	

<b>2.5. For the policy to be given effect by this Bill, is there analysis available on:</b>	
<b>(a) the size of the potential costs and benefits?</b>	NO
<b>(b) the potential for any group of persons to suffer a substantial unavoidable loss of income or wealth?</b>	NO
A formal cost/benefit analysis was not carried out, but analysis was carried out to identify the problem and its implications. This material will be available on the Ministry of Business, Innovation and Employment website.	

<b>2.6. For the policy to be given effect by this Bill, are the potential costs or benefits likely to be impacted by:</b>	
<b>(a) the level of effective compliance or non-compliance with applicable obligations or standards?</b>	NO
<b>(b) the nature and level of regulator effort put into encouraging or securing compliance?</b>	NO

## Part Three: Testing of Legislative Content

### Consistency with New Zealand's international obligations

<b>3.1. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with New Zealand's international obligations?</b>
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The Ministry of Foreign Affairs and Trade was consulted to check that the Bill is consistent with NZ's international obligations. In addition, the Guardians are required under the Bill, to avoid prejudice to New Zealand's reputation as a responsible member of the world community with respect to the investment of the Venture Capital Fund.

### Consistency with the government's Treaty of Waitangi obligations

<b>3.2. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with the principles of the Treaty of Waitangi?</b>
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No formal steps have been taken but there are no obvious areas where the intended amendments would potentially conflict with the principles of the Treaty of Waitangi.

### Consistency with the New Zealand Bill of Rights Act 1990

<b>3.3. Has advice been provided to the Attorney-General on whether any provisions of this Bill appear to limit any of the rights and freedoms affirmed in the New Zealand Bill of Rights Act 1990?</b>	YES
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<https://www.justice.govt.nz/justice-sector-policy/constitutional-issues-and-human-rights/bill-of-rights-compliance-reports/advice/>

### Offences, penalties and court jurisdictions

<b>3.4. Does this Bill create, amend, or remove:</b>	
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<b>(a) offences or penalties (including infringement offences or penalties and civil pecuniary penalty regimes)?</b>	NO
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<b>(b) the jurisdiction of a court or tribunal (including rights to judicial review or rights of appeal)?</b>	NO
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### Privacy issues

<b>3.5. Does this Bill create, amend or remove any provisions relating to the collection, storage, access to, correction of, use or disclosure of personal information?</b>	NO
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### External consultation

<b>3.6. Has there been any external consultation on the policy to be given effect by this Bill, or on a draft of this Bill?</b>	YES
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Stakeholders, including fund managers, investors, founders, government delivery and implementation partners were consulted in 2018 on the state of the early stage capital markets in New Zealand. The key issue from this consultation was the view that there was a gap in New Zealand's series A&B venture capital market.

The draft Bill was prepared with detailed consultation with the Guardians and NZVIF.

### Other testing of proposals

<b>3.7. Have the policy details to be given effect by this Bill been otherwise tested or assessed in any way to ensure the Bill's provisions are workable and complete?</b>	<b>YES</b>
Officials have prepared a draft policy statement to help test the provisions of the Bill that relate to the policy directions and definitions to be contained in a policy statement, and intend to consult stakeholders on this draft policy statement.	

## Part Four: Significant Legislative Features

### Compulsory acquisition of private property

4.1. Does this Bill contain any provisions that could result in the compulsory acquisition of private property?	NO
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### Charges in the nature of a tax

4.2. Does this Bill create or amend a power to impose a fee, levy or charge in the nature of a tax?	NO
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### Retrospective effect

4.3. Does this Bill affect rights, freedoms, or impose obligations, retrospectively?	NO
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### Strict liability or reversal of the usual burden of proof for offences

4.4. Does this Bill:	
(a) create or amend a strict or absolute liability offence?	NO
(b) reverse or modify the usual burden of proof for an offence or a civil pecuniary penalty proceeding?	NO

### Civil or criminal immunity

4.5. Does this Bill create or amend a civil or criminal immunity for any person?	NO
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### Significant decision-making powers

4.6. Does this Bill create or amend a decision-making power to make a determination about a person's rights, obligations, or interests protected or recognised by law, and that could have a significant impact on those rights, obligations, or interests?	NO
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### Powers to make delegated legislation

4.7. Does this Bill create or amend a power to make delegated legislation that could amend an Act, define the meaning of a term in an Act, or grant an exemption from an Act or delegated legislation?	NO
Although the Bill does not include a power to make delegated legislation, the Bill does require the Minister to give a policy statement, and while this policy statement will not be delegated legislation, the policy statement will influence how the Guardians will operate under the Act.	

<b>4.8. Does this Bill create or amend any other powers to make delegated legislation?</b>	NO
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**Any other unusual provisions or features**

<b>4.9. Does this Bill contain any provisions (other than those noted above) that are unusual or call for special comment?</b>	YES
<p>Schedule 1 of the Bill puts a requirement on the Guardians and NZVIF to enter into an arrangement using reasonable efforts, such that NZVIF would invest the VCF in a number of private venture capital funds, while the Guardians will provide oversight, monitoring, and ultimately be accountable for the VCF.</p> <p>If these reasonable efforts are not successful, the Minister of Finance may specify a contract or other arrangement that will be binding on the Guardians and NZVIF. The parties will still have the right to cancel or amend the agreement in accordance with the terms of the agreement (which we expect to reflect normal commercial practice).</p> <p>The bringing together of parties into an agreement in this way is unusual. However, the Guardians and NZVIF are both Crown Entities and so this represents government making decisions on how it organises itself.</p>	