

Strategopoly: playing with the nation's assets

Air New Zealand in 2001; Auckland International Airport and KiwiRail in 2008 ... the New Zealand government has on at least three occasions in the not-so-distant past intervened in private market transactions to secure for itself, or place limitations upon, who can own or control so-called 'strategic assets'. And in recent months the 'strategic asset' label has been applied to dairy farms¹ in order to justify restrictions on foreign ownership. Dave Heatley and Bronwyn Howell ask what characteristics of an asset make it strategic, particularly in the national policy context.

The answer to this question is important. It pertains directly to the circumstances in which it is appropriate for the government, rather than private individual or corporations, to own and control the asset – especially when government assumption of control disadvantages those individuals and corporations. A cynical view often expressed² is that an asset becomes strategic simply when it suits politicians to regard it so – giving rise to the risk that they might over-use their powers of compulsion in declaring assets strategic, and make declarations for political rather than public-good purposes. However, whether or not an asset is strategic comes down to a wider question: what objective is served by control of that asset?

The asset game

'Strategy' is a concept most closely associated with the military, games and business. In these spheres the meaning of 'strategic asset' is straightforward: an asset is strategic if *control* over that asset is essential to achieving a particular and well-defined objective – that is, there is no other alternative means of securing the desired outcome. This makes the relevant asset a 'must have' rather than just 'nice to have'.³

Control may mean a variety of things. But the important considerations in its meaning are the right to use the asset – and the right to *exclude opponents from using it*, which thus limits their strategy choices. It is also important to distinguish between simple possession of an asset ('ownership') and control of a bundle of rights associated with the use of the asset.⁴ For example, I may 'own' my land but my ability to do whatever I like with it is significantly constrained by the fact that others (such as

¹ See D Heatley and B Howell (2010) 'Regulatory restrictions down on the farm' *Competition and Regulation Times* issue 32 p4 (also available at www.iscr.org.nz).

² See for example *The New Zealand Herald* (2008) 'Strategic asset only if it suits' editorial 30 April.

³ Political motivations notwithstanding, it could be argued that the 2008 government purchase of KiwiRail did indeed secure a strategic asset, in that operational control was considered crucial to the fulfilment of the then government's transport-strategy objectives and was unobtainable via any other legislative or contractual means.

⁴ L Evans, N Quigley and K Counsell (2009) 'Protection of Private Property Rights and Just Compensation: An Economic Analysis of the Most Fundamental Human Right Not Provided in New Zealand' (available at www.iscr.org.nz).

my bank, which holds the mortgage; or my local authority, which has obligations under the Resource Management Act) control many of my rights of use.

Ultimately, it is the control of specific rights rather than possession of the physical asset that is essential for achieving a strategic objective. This control can be acquired in many ways: for example through conquest, purchase, contractual agreement, or control by allies.

From a public policy perspective, what makes an asset strategic should follow from its role in achieving a given objective. During wars or national emergencies, governments may deem it necessary to make compulsory acquisitions of (for example) land and transportation networks in order to guarantee the country's defence. In other situations, control may be necessary in order to deliver net public benefits – such as acquiring land to build a road or electricity distribution grid, the benefits from which (net of compensation paid to the original owner) exceed the costs.

Furthermore, where assets are physically located within New Zealand, the government has access to legislative and regulatory mechanisms by which it can obtain control of strategic assets.⁵ Although in some circumstances (such as under the Public Works Act) the government is required to compensate the original owner when it assumes control rights, in most other cases the government can assume control by dint of 'executive action' for which no compensation is paid – for example, when it limits the types of house renovations that can be carried out in areas covered by historic preservation orders⁶ or when it requires incumbent telecommunications network operators to share their assets with rival firms⁷).

Playing two game(s)

The Local Government Act 2002 defines a strategic asset as any asset held by a local authority which is deemed necessary for maintaining that authority's capacity to achieve or promote any outcome that it determines to be important to the current or future wellbeing of its community. The Act further defines two particular strategic assets: equity holdings in any port or airport company; and land or buildings required to provide affordable housing.

The means of assessing the current or future wellbeing of the community is not specified, offering local authorities considerable discretion in determining both their objectives and the strategic assets required to realise these objectives. Nor does the Act distinguish between possession of an asset and the control rights associated with that asset. For example, shares held in ports and airports are automatically deemed strategic even when they amount to a minority stakeholding that confers no ability to exert effective control of the port or airport.

⁵ These mechanisms are, of course, unavailable to businesses or individuals.

⁶ D Heatley (2009) 'Non-compensation – it's not just' *Competition and Regulation Times* issue 29 p14 (also available at www.iscr.org.nz).

⁷ B Wilkinson (2008) 'A Primer on Property Rights, Takings and Compensation' (available at www.wgtn-chamber.co.nz).

Furthermore, once statutory processes have been invoked to declare an asset strategic, the local authority is required to consult with its community if it ever wants to dispose of that asset. This obligation for community consultation, combined with the considerable discretion given to a local authority in setting its objectives, opens up the opportunity for assets to be declared strategic as a way of increasing the difficulty for any future authority to dispose of assets that were deemed essential for delivering the policies (both public-good-oriented and self-serving) of its predecessors. So a specific policy – which may be only one of many ways of delivering a given public-good objective – can become ‘locked in’ for extended periods by one set of politicians in order to frustrate their political opponents.

When making a determination under the Overseas Investment Act 2005, ministers are required by regulation 28(h) to consider whether a proposed overseas investment will, or is likely to, assist New Zealand in maintaining control of strategically sensitive infrastructure on sensitive land.

‘Strategically sensitive infrastructure’ is not defined, so unlike the Local Government Act, the Overseas Investment Act provides no clear process by which such assets can be specifically identified as, or declared to be, strategic. This regulation is invoked only when overseas entities (essentially any entity where more than 25% of the control is held by non-New-Zealand entities) seek to purchase more than 25% of the relevant asset. It was introduced in March 2008, when the government sought the means to decline approval for the Canadian Pension Plan Investment Board’s proposed purchase of 40% of the shares of Auckland International Airport Limited.

Control freaks

Although the focus of the Overseas Investment Act is the ownership of assets (particularly land) located in New Zealand, regulation 28(h) makes a clear statement about the importance of control. This would appear to address the distinction between mere possession of an asset and the ability to make decisions about its use. Regulation 28(h) allows foreign investment if it assists ‘New Zealand’ (the state, as custodian of the national interest) in maintaining control of the ‘strategic asset’.

However, if the asset is already in private ownership, the private owner can sell only those residual rights over which the state does not already exercise formal control via other legislative instruments. The foreign purchaser of, for example, a farm business would be subject to the same environmental and animal protection laws as a New Zealand owner. It is difficult to see how any foreign investment could ever assist in altering the extent of formal state control of a privately-held asset. However, if there is an implicit assumption that control of those remaining rights by a private New Zealander in some way acts as an unwritten proxy for the exertion of control by the state in its pursuit of the objective for which the asset is a strategic necessity (that is, the state has gained control of the relevant rights via an unwritten ‘alliance’ with the New Zealand owners), then a transfer to foreigners will dilute that informal control – and hence will dilute the Government’s ability to achieve its objective.

Nevertheless, an unwritten alliance provides no certainty that even a New Zealand owner will always exercise the residual control rights in a manner consistent with the Government’s objectives. If control of the remaining rights is truly essential to delivering the objective and there is no alternative

means of doing so, and if the rights are ‘strategic’ and an unwritten alliance involves risks in achieving the objective, then the government should acquire them.

Possession of a ‘strategic asset’ may be 9/10ths of the law, and control may confer 100% of the ability to achieve strategic objectives – but neither guarantees that the strategy is worth pursuing in the first place.

Bronwyn Howell is ISCR’s General Manager; **Dave Heatley** is a research fellow at ISCR.