

# The Treasury

## Reform of the Overseas Investment Act Information Release

July 2020

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- [34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
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## Treasury Report: Overseas Investment Act Phase 2 reforms: package of reform

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<b>Date:</b>	5 August 2019	<b>Report No:</b>	T2019/1649
		<b>File Number:</b>	IM-5-3-8 (Overseas Investment Act Phase Two)

### Action Sought

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	Action Sought	Deadline
Hon David Parker <b>Associate Minister of Finance</b>	<b>Indicate</b> your preferred reform options.  <b>Refer</b> this paper to the Associate Minister of Finance (Hon. David Clark), the Minister for Land Information and the Minister of Fisheries.	Thursday 8 <sup>th</sup> August
Hon Grant Robertson <b>Minister of Finance</b>	<b>Note</b> the contents of this report.	Friday 16 <sup>th</sup> August

### Contact for Telephone Discussion (if required)

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Name	Position	Telephone	1st Contact
Megan Noyce	Principal Advisor, International	[39]	[23] ✓
[39]	Senior Analyst, International	[39]	N/A

### Actions for the Minister's Office Staff (if required)

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**Return** the signed report to Treasury.

**Refer** to the Associate Minister of Finance (Hon. David Clark), the Minister for Land Information, and the Minister of Fisheries.

Note any feedback on the quality of the report

# Treasury Report: Overseas Investment Act Phase 2 reforms: package of reform

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## Executive Summary

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### Purpose

This report seeks your decisions on the design of a reform package for the Phase 2 review of the Overseas Investment Act 2005 (the Act). It recommends options for reform, developed following public consultation in April and May 2019. Cabinet has invited you to report back in October 2019 with reform proposals.

We have copied this report to the Minister of Finance for his information and future discussion as proposals are finalised for Cabinet consideration.

### The case for reform

Overseas investment can bring benefits including job creation, access to international markets, and the introduction of new technologies and processes that can lift productivity. However, there is evidence that the Act's complexity and scope is discouraging the investment New Zealand needs.

At the same time, overseas investment can pose significant risks – including risks to national security and public order. The Act does not allow the Government to decline such transactions. These reforms provide an opportunity to address issues, including:

- **That the consent framework is complex and creates uncertainty.** The *investor test* (which generally applies to all transactions and assesses an investor's competency and capacity) and the *benefit to New Zealand test* (the benefits test – which applies to transactions involving sensitive land and fishing quota) seek to ensure that overseas investment will be beneficial, but require investors to provide a significant amount of information of often limited value.
- **Gaps in the screening regime.** There is limited capacity to consider implications for New Zealand's national security or public order and ambiguity about the extent to which potential harms to New Zealand's economy, and other national interests, can be factored into decision-making under the Act.
- **The disproportionate cost of screening lower risk investments.** Screening investments such as the purchase or leases of land only because it is adjoins to land with sensitive characteristics, medium-term leases, fundamentally New Zealand entities and transactions that do not change the control of sensitive assets, impose disproportionate compliance costs on applicants relative to the risks being managed.

## **The recommended reform package**

Following stakeholder engagement and further policy development, we have developed a recommended reform package (the recommended package) that seeks to address the Act's primary issues. We have also included alternative options that generally put greater emphasis on the government's ability to manage the risks of overseas investment, although some of these options come at significant expense to the regime's predictability and certainty.

The recommended package includes:

*An improved consent framework that will simplify the consent process for most transactions*

Our proposals aim to increase effectiveness and reduce uncertainty by:

- narrowing and simplifying the investor test;
- simplifying the benefits test, which reduces the number of factors without shrinking coverage;
- introducing a new 'backstop' national interest test; and
- introducing statutory timeframes for deciding applications, tailored to application type.

The alternative options include an investor test that provides decision-makers with more discretion than the recommended package, a benefits test that enables consideration of some negative effects, and no statutory timeframes.

*Minor changes to both strengthen and clarify the criteria for consent:*

- allowing recognition of protections for wāhi tūpuna, Māori reservations, and access for cultural purposes, within the benefits test; and
- removing farm land advertising requirements.

The alternative options allow consideration under the benefits test of an investment's effect on tax revenue and, for investments involving water bottling or bulk water extraction for human consumption, the effect on water quality and sustainability. It would also clarify rather than remove the farm land advertising requirements.

*Removing some lower risk transactions from screening:*

- reducing the amount of land screened only because it adjoins sensitive land;
- raising the threshold for screening non-freehold interests in land (e.g. leases and profits-à-prendre), other than residential land, to 15 years or more (from the current three years); and
- a range of changes to who and when we screen, including removing from screening investors that are fundamentally New Zealand entities, and transactions where the control of an asset does not materially change.

The alternative options generally remove fewer transactions from screening.

## **The Act's complexity affects both design and implementation**

The recommended package provides a cohesive set of reforms. The alternative options presented for most issues could be adopted in place of specific recommended options. However, for some issues there are interdependencies between specific topics or sub-topics requiring consideration as a package. This includes options to improve the consenting framework and the recommended changes to reduce the number of low risk transactions and

New Zealand entities screened. We have indicated where, if you wish to explore alternative combinations of reforms, we will need to provide additional advice about impacts across the package as a whole.

The options you are considering affect every part of the Act. The complexity of the Act, and scale of the proposed reform package, will present significant challenges as we work through detailed design and drafting. The ambitious timeframe <sup>[34]</sup>

We will work closely with Land Information New Zealand (LINZ) and other affected agencies on detailed policy design, and to identify a reasonable implementation period, once you have confirmed your preferred package.

### **Next steps**

You are meeting with us on 8 August 2019 to discuss this advice. We recommend that you discuss reform options with relevant ministerial colleagues (e.g. decision-making ministers under the Act). You are meeting with the Minister for Land Information and the Associate Minister of Finance (Hon. David Clark) on 22 August 2019.

This report does not address:

- whether the ministerial directive relating to rural land should be enshrined in the Act (we will discuss this further when we meet with you on 8 August);
- the offer back of special land to the Crown;
- the proposal to introduce a national security and public order call-in power;
- the Overseas Investment Office's enforcement powers (including the enforcement powers required to operationalise the call-in power); or
- the role of judicial review in relation to proposals to introduce a national interest test and call-in power.

We will provide advice on these issues later this month. Your decisions on these issues will be reflected in the full package of reform provided to Cabinet.

The Government has indicated it intends to enact these reforms by mid-2020. To achieve this, the proposed reforms will need to be considered by Cabinet by the end of October. Key milestones to meet this timeframe are set out below.

### *Key upcoming dates*

Draft Cabinet paper to your office	12 September
Cabinet paper required to be submitted to Cabinet Office	17 October
Cabinet paper at DEV	23 October
Cabinet	29 October

## Recommended Action

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We recommend that you:

- a **agree** to the Treasury developing a draft Cabinet paper for your consideration recommending amendments to the Overseas Investment Act 2005;  
  
*agree / disagree*
- b **indicate** your preferred reform options in Tables 1, 2 and 3 to be included in the draft Cabinet paper;
- c [1, 36]

*noted*

- d **note** that the recommended package provides a cohesive set of reforms. For some issues we have indicated where, if you wish to explore alternative combinations of reforms, we will need to provide additional advice about impacts across the package as a whole;

*noted*

- e **note** that maintaining the status quo is also an option for all issues set out in Tables 1, 2 and 3;

*noted*

- f **refer** this paper to the Associate Minister of Finance (Hon David Clark) and the Minister for Land Information;

*referred / not referred*

- g **refer** this paper to the Minister of Fisheries, as the recommended reform package should also be reflected in the overseas investment fishing provisions in the Fisheries Act 1996, to ensure consistency across the overseas investment screening regime.

*referred / not referred*

Megan Noyce  
**Principal Advisor, International**

Hon David Parker  
**Associate Minister of Finance**

Hon Grant Robertson  
**Minister of Finance**

Please circle your preferred options

**Table 1: Proposals for the consenting framework (corresponds to section 4)**

Problem	Recommended option	Alternative option/s	Minister comment
<b>How should we test an investor's suitability to invest in New Zealand? [Section 4.1]</b>			
The investor test lacks a clear purpose, which can result in ambiguity for decision-makers and investors.	Introduce a purpose statement for the test.  <b>agree/disagree</b>		
The broad definitions of Relevant Overseas Person (ROP) or Individuals With Control (IWC) can result in uncertainty and a perception that the test captures individuals who, in practice, have limited involvement with the prospective investments.	Note that additional clarification on ROP/IWC selection can be provided operationally.  <b>noted</b>		
The test applies to New Zealanders identified as ROPs or IWC, despite New Zealanders being able to acquire sensitive assets without consent.	Exclude New Zealanders identified as ROP/IWCs from the investor test.  <b>agree/disagree</b>		
Repeat investors are required to satisfy the test with every investment. This is disproportionate to the risks being managed.	Introduce a 'standing consent' which exempts ROP/IWCs from the investor test if they have previously satisfied the requirements, unless there have been changes to their character and capability (the notification of which would be mandatory).  <b>agree/disagree</b>  <i>Note that if you disagree with the proposal to remove the financial commitment and business acumen criteria from the investor test, these criteria would need to be satisfied for each new investment.</i>		
The good character criterion is broad and imposes costs disproportionate to the risks posed by most investors.	Remove the requirement to consider, as a reflection of individual character, contraventions and offences by, or allegations against, entities in which an ROP/IWC has a significant interest (e.g. an entity they own securities in).  <b>agree/disagree</b>		
	Remove the requirement to consider "any other matter that reflects adversely on the person's fitness to have the particular overseas investment".  <b>agree/disagree</b>		
	Only consider offences and contraventions that are relevant, and list these in the Act or Regulations (for example criminal offences punishable by a term of imprisonment and civil contraventions resulting in pecuniary penalties and enforceable undertakings, in any jurisdiction).  <b>agree/disagree</b>	Only consider offences and contraventions that are relevant but allow decision-makers to determine relevance.  <b>agree/disagree</b>	
	Only consider allegations relating to relevant offences or contraventions for which official proceedings have commenced, in any jurisdiction.  <b>agree/disagree</b>	Only consider allegations relating to relevant offences or contraventions for which official proceedings or official investigations have commenced, in any jurisdiction.  <b>agree/disagree</b>	
Referring to section 15 of the Immigration Act criteria duplicates the current good character criterion.	Remove the reference to section 15 of the Immigration Act.  <b>agree/disagree</b>		

Problem	Recommended option	Alternative option/s	Minister comment
The financial commitment criterion is broad and of limited value (no applicant has ever been declined on this ground). As such, it imposes costs that are disproportionate to the risks posed by most investors.	Remove the financial commitment criterion.  <b>agree/disagree</b>	<i>Note that if you prefer to maintain the status quo, this criterion would need to be satisfied for each new investment even if investors have a standing consent (if you agree to the standing consent proposal).</i>	
The business experience and acumen criterion is broad and disproportionate to the risks being managed.	Replace business experience and acumen criterion with an objective assessment of relevant factors such as undischarged bankruptcies and disqualifications.  <b>agree/disagree</b>	Maintain current business experience and acumen criterion and add the consideration of relevant factors such as undischarged bankruptcies and disqualifications.  <b>agree/disagree</b>  <i>Note that if you prefer this option, this criterion would need to be satisfied for each new investment, even if investors have a standing consent (if you agree to the standing consent proposal).</i>	
Decision-makers are unable to consider the character of the corporate entity/entities involved in the investment (other than where corporate actions can be imputed to the character of the individual investor, noting we have recommended removing this part of the investor test).	Allow targeted consideration of corporate character in the investor test. This would be limited to:  <ul style="list-style-type: none"> <li>• considering offences or contraventions (e.g. to criminal offences punishable by imprisonment and civil contraventions resulting in pecuniary penalties and enforceable undertakings);</li> <li>• by entities which have substantive control over the investment.</li> </ul> <b>agree/disagree</b>		
The investor test imposes costs disproportionate to risks posed by the majority of investors.	Maintain status quo where decision-maker considers, and decides on, the investor's suitability to invest, before consent is granted.  <b>agree/disagree</b>	Shift to a post-consent model for the investor test where investors declare they are suitable to invest and enforcement action can be taken if they are later found unsuitable to invest.  <b>agree/disagree</b>	

Problem	Recommended option	Alternative option/s	Minister comment
<b>How should benefit to New Zealand be determined? [4.2.1]</b>			
<i>Note that if you wish to explore alternative combinations of reforms within this section, we will need to provide additional advice about impacts across the package as a whole.</i>			
<p>The benefits test assesses applications to acquire sensitive land and fishing quota against a large number of (potentially overlapping) factors. This creates significant compliance costs and uncertainty for investors. There is ambiguity about whether an investment's negative effects can be considered when applying this test.</p>	<p>Determine whether investments to acquire sensitive land are of benefit to New Zealand by considering their effect against a:</p> <ul style="list-style-type: none"> <li>• broad economic factor;</li> <li>• broad environmental factor;</li> <li>• general public access factor;</li> <li>• historic heritage factor;</li> <li>• factor relating to advancement of significant Government policies,</li> <li>• factor relating to New Zealanders' involvement in the relevant investment; and</li> <li>• factor recognising any other consequential benefits of the investment.</li> </ul> <p>Clarify that Ministers cannot consider the negative effects of an investment under this test.</p> <p>Remove the ability to add to this list of factors via Regulations.</p> <p style="text-align: right;"><b>agree/disagree</b></p> <p>Note that decisions you make relating to whether to consider an investment's effect on water, tax revenue, or Māori cultural values [in Section 5] may expand this list of factors.</p> <p style="text-align: right;"><b>noted</b></p> <p>Note that offering back special land to the Crown is currently a benefits test factor. We will provide you with further advice regarding the treatment of special land. Your decisions on this advice will inform the design of the benefits test.</p> <p style="text-align: right;"><b>noted</b></p>	<p>The same as the recommended option, but clarify that Ministers can consider the negative effects of an investment on public access under this test.</p> <p style="text-align: right;"><b>agree/disagree</b></p> <p><i>Note that the alternative options for water extraction and tax revenue would also allow consideration of negative effects in the benefits test.</i></p>	<b>noted</b>

Problem	Recommended option	Alternative option/s		Minister comment
<p>There is no ability to decline investments that are contrary to New Zealand's national interest because, for example, they pose significant risks to national security or public order.</p>	<p>Introduce a 'national interest' test that can apply to any investment screened under the Act that poses significant risks.</p> <p>Design features include:</p> <ul style="list-style-type: none"> <li>• a separate decision-maker (not the Minister ordinarily responsible for assessing the particular application);</li> <li>• the investment would be declined if it is contrary to New Zealand's national interest, having regard to: risks to national security, public order, international relations, the economy, the environment and other national interests; the degree to which these risks can be mitigated; any benefits associated with the transaction; and New Zealand's international obligations;</li> <li>• the test would automatically apply to investments: where foreign governments have a greater than 10% interest; that present national security risks; and in specified strategically important industries and high-risk critical national infrastructure;</li> <li>• the test could be applied to other transactions on recommendation by the ordinary decision-making Minister and with agreement from the Minister responsible for exercising the national interest test; and</li> <li>• decisions made under the test would be made public, with exceptions for information necessary to protect national security, international relations, or commercial-in-confidence information.</li> </ul> <p style="text-align: right;"><i>agree/disagree</i></p>			
<b>How should an investment's level of benefit be assessed (counterfactual)? [Section 4.2.2]</b>				
<p>Decision-makers currently determine whether an investment in land is beneficial by considering what is likely to happen if the investment does not proceed (the counterfactual test). This is a theoretical assessment and there is a high degree of subjectivity in determining the appropriate counterfactual, creating uncertainty for applicants.</p>	<p>Determine whether an investment in land is beneficial by considering the state of the land (and activities on it) at the time that the application is lodged (that is, the current state).</p> <p style="text-align: right;"><i>agree/disagree</i></p>	<p><b>[Alternative]</b></p> <p>Determine whether an investment in land is beneficial by considering what is likely to happen if the vendor continues to own it.</p> <p style="text-align: right;"><i>agree/disagree</i></p>	<p><b>[Alternative or complement]</b></p> <p>Consent to a transaction between two overseas persons ('no detriments test') as long as the vendor had previously obtained consent, existing benefits and conditions will be maintained, and the purchaser does not gain a greater level of control over the asset.</p> <p style="text-align: right;"><i>agree/disagree</i></p>	
<b>Ensuring benefit is proportionate [Section 4.2.3]</b>				
<p>Benefits for investments in non-urban land larger than five hectares must be 'substantial and identifiable', which adds complexity and significant uncertainty. There is no explicit legislative basis for requiring benefits to be proportional to an asset's sensitivity for any other asset type.</p>	<p>Require all investments in land to offer benefits proportional to the sensitivity of the land and the interest acquired. Remove the 'substantial and identifiable' threshold for non-urban land greater than five hectares.</p> <p style="text-align: right;"><i>agree/disagree</i></p>			

Problem	Recommended option	Alternative option/s	Minister comment
<b>Should statutory timeframes be introduced into the Act? [Section 4.3]</b>			
No statutory timeframes in which applications must be assessed. Decision-making timeframes are unpredictable and considerably longer than in comparable jurisdictions.	<p>Introduce tailored deadlines for decision-making under each consent pathway, to increase predictability and transparency, and signal the depth of enquiry expected.</p> <p>Provide the OIO with an initial period to review an application, and the ability to request further information, before accepting an application.</p> <p>Allow decision-makers to extend the deadline once (either by a proscribed or agreed period).</p> <p>Require decision-makers to report on compliance with statutory timeframes to promote public accountability.</p> <p>Provide that a breach of the statutory timeframe will not render the decision itself unlawful, and the Crown would not be liable for any loss suffered by an applicant resulting from a breach.</p> <p style="text-align: right;"><i>agree/disagree</i></p>		

**Table 2: Proposals to strengthen the criteria for consent (corresponds to section 5)**

Problem	Recommended option	Alternative option/s	Alternative option/s	Minister comment
<b>Should a factor to address water extraction be included in the benefits test? [Section 5.1]</b>				
There is limited ability to consider an investment's effect on water quality or sustainability when considering whether to grant consent.	<p>Maintain the status quo.</p> <p style="text-align: right;"><i>agree/disagree</i></p> <p>Note that an investment's positive impact on water quality and sustainability could be considered through the broad environmental factor if the recommended benefits test option is adopted.</p> <p style="text-align: right;"><i>noted</i></p>	<p><b>[Alternative]</b></p> <p>Include a factor in the recommended benefits test that considers whether an investment that involves water bottling or bulk water extraction for human consumption will have a positive effect on water quality or sustainability.</p> <p style="text-align: right;"><i>agree/disagree</i></p> <p><i>Note that this option is viable regardless of whether the recommended (positively framed) benefits test option or the alternative benefits test option is adopted.</i></p>	<p><b>[Alternative]</b></p> <p>Include a factor in the alternative benefits test that considers whether an investment that involves water bottling or bulk water extraction for human consumption will have a positive or negative effect on water quality or sustainability.</p> <p style="text-align: right;"><i>agree/disagree</i></p> <p><i>Note that this option is only viable if the alternative benefits test option (enabling limited consideration of negative effects) is adopted.</i></p>	

Problem	Recommended option	Alternative option/s		Minister comment
<b>Should tax be considered as part of the consent process? [Section 5.2]</b>				
<p>There is a limited ability to consider the implications of an investment for New Zealand's tax revenue. Past tax compliance can be considered as part of the investor test.</p>	<p><i>Maintain the status quo:</i> relevant tax offences and contraventions resulting in a pecuniary penalty would continue to be considered under the investor test.</p> <p style="text-align: right;"><b>agree/disagree</b></p> <p>Note that we are still considering whether significant civil tax penalties imposed by a tax authority rather than a court (such as shortfall penalties for tax evasion) should be covered in the investor test.</p> <p style="text-align: right;"><b>noted</b></p>	<p>Either, in <b>addition</b> to the recommended option, include a factor in the benefits test that relates to whether an investment will have a positive effect on New Zealand's income tax revenue with respect to the investment.</p> <p style="text-align: right;"><b>agree/disagree</b></p> <p><i>Note that this option is viable regardless of whether the recommended (positively framed) benefits test option or the alternative benefits test option is adopted.</i></p>	<p>Or, in <b>addition</b> to the recommended option, include a factor in the alternative benefits test that relates to whether an investment will either have a positive effect on, or present a risk to, New Zealand's tax revenue.</p> <p style="text-align: right;"><b>agree/disagree</b></p> <p><i>Note that this option is only viable if the alternative benefits test option (enabling limited consideration of negative effects) is adopted.</i></p>	
<b>Should a factor addressing Māori cultural values be included in the benefits test? [Section 5.3]</b>				
<p>The Act allows limited consideration of Māori cultural values (as part of the historic heritage factor) in the benefits test, however there are concerns that this is not sufficient.</p>	<p>Clarify and broaden the benefits test to allow recognition of protections for wāhi tūpuna or Māori reservations on sensitive land.</p> <p style="text-align: right;"><b>agree/disagree</b></p> <p>Broaden benefits test to allow recognition of provision of public access for the purposes of the stewardship of historic heritage and natural resources.</p> <p style="text-align: right;"><b>agree/disagree</b></p> <p>Note that the recommended option for sensitive adjoining land will continue to screen some land significant to Māori.</p> <p style="text-align: right;"><b>noted</b></p>			
<b>Should the requirement to advertise farm land be removed or improved? [Section 5.4]</b>				
<p>Transactions can be entered into before farmland is advertised. The Act does not say when exemptions should be granted. Minimum advertising standards are ineffective.</p>	<p>Remove the requirement to advertise farm land.</p> <p style="text-align: right;"><b>agree/disagree</b></p> <p>Note that our assessment of criteria shows that the options of removing, or improving the farm land advertising, are finely balanced. There are also legitimate policy objectives for retaining and clarifying the requirement.</p> <p style="text-align: right;"><b>noted</b></p>		<p>Require advertising before a transaction, improve exemptions, and modernise minimum advertising requirements</p> <p style="text-align: right;"><b>agree/disagree</b></p>	

<i>Problem</i>	<i>Recommended option</i>	<i>Alternative option/s</i>	<i>Minister comment</i>
[4]			

**Table 3: Proposals to reduce the screening of low risk investment (corresponds to section 6)**

<i>Problem</i>	<i>Recommended option</i>	<i>Alternative option</i>	<i>Minister comment</i>
<b>How should the Act treat sensitive adjoining land? [6.1]</b>			
The Act screens land adjoining sensitive land even if that land is of low environmental, historic or cultural value and there are no access concerns. This is disproportionate to the risks being managed.	<p>Remove all categories of sensitive adjoining land from the Act, with the exception of land adjoining:</p> <ul style="list-style-type: none"> <li>• foreshore;</li> <li>• lakebeds;</li> <li>• a Māori reservation that adjoins the sea or a lake and to which section 340 of the Te Ture Whenua Māori Act 1993 applies;</li> <li>• land that is set apart as a Māori reservation and that is wāhi tapu under section 338 of Te Ture Whenua Māori Act 1993; and</li> <li>• wāhi tapu or a wāhi tapu area under the Heritage List/Act.</li> </ul> <p>Include the following new categories of land significant to Māori previously covered by section 37 in Table 2:</p> <ul style="list-style-type: none"> <li>• reserves that are subject to the Reserves Act 1988 and are managed wholly or jointly by the governance entity of a collective group of Māori such as an iwi or hapū; and</li> <li>• public conservation land that has been used as cultural redress in Treaty settlements and has retained conservation protection.</li> </ul> <p style="text-align: right;"><i>agree/disagree</i></p> <p>[1, 36]</p> <p style="text-align: right;"><i>noted</i></p>	<p>Remove one category of sensitive adjoining land from the Act - "land that is listed, or in a class listed, as a reserve, a public park, or other sensitive area by the regulator under section 37".</p> <p>Include the following categories of land previously covered by section 37 in Table 2:</p> <ul style="list-style-type: none"> <li>• national parks;</li> <li>• scientific, scenic, historic or nature reserves under the Reserves Act 1977 managed by local authorities and others (in addition to those administered by the Department of Conservation);</li> <li>• wildlife management reserves, refuges and sanctuaries under the Wildlife Act 1953;</li> <li>• reserves that are subject to the Reserves Act 1988 and are managed wholly or jointly by the governance entity of a collective group of Māori such as an iwi or hapū; and</li> <li>• public conservation land that has been used as cultural redress in Treaty settlements and has retained conservation protection.</li> </ul> <p style="text-align: right;"><i>agree/disagree</i></p> <p>[1, 36]</p> <p style="text-align: right;"><i>noted</i></p>	

Problem	Recommended option	Alternative option	Minister comment
<b>How should the Act treat leases and other less than freehold interests in land? [6.2]</b>			
<p>The Act screens leases and other less-than freehold interests in sensitive land with terms of three years or more. This is disproportionate to the risks being managed.</p>	<p>Screen leases and other less-than freehold interests with terms of 15 years or more. Leases and other less-than freehold interests in residential land of three years or more would continue to be screened.</p> <p style="text-align: right;"><i>agree/disagree</i></p> <p>[1, 36]</p> <p style="text-align: right;"><i>noted</i></p>	<p><b>[Alternative]</b></p> <p>Screen leases and other less-than freehold interests with terms of 10 years or more. Leases and other less-than freehold interests in residential land of three years or more would continue to be screened.</p> <p style="text-align: right;"><i>agree/disagree</i></p> <p>[1, 36]</p> <p style="text-align: right;"><i>noted</i></p>	<p><b>[Complement]</b></p> <p>Screen cumulative leases and other less-than freehold interests that, in total, exceed the relevant screening threshold.</p> <p style="text-align: right;"><i>agree/disagree</i></p> <p>Note that this option could be adopted as a complement to either a 15 or 10 year screening threshold.</p> <p style="text-align: right;"><i>noted</i></p> <p>[1, 36]</p> <p style="text-align: right;"><i>noted</i></p>
<p>There is a risk that Phase 1 amendments to clarify the status of periodic leases of residential land imply that other periodic leases must be screened.</p>	<p>Clarify that periodic leases do not require screening.</p> <p style="text-align: right;"><i>agree/disagree</i></p>		

Problem	Recommended option	Alternative option	Minister comment
<b>Excluding fundamentally New Zealand entities from the scope of the Act [6.3]</b>			
<p>Note that this package of reforms is designed to work coherently to address the identified problems. If Ministers have concerns with any aspect of the package, we will need to discuss how changes to one element might affect the package as a whole.</p> <p style="text-align: right;"><i>noted</i></p>			
<p>A body corporate is an overseas person if it is 25% owned or controlled by overseas person, even if the body corporate is majority owned and controlled by New Zealanders. This is disproportionate to the risks being managed.</p>	<p>Narrow the definition of “overseas person” to exclude New Zealand incorporated and listed bodies corporate that are majority owned and controlled by New Zealanders.</p> <p>A New Zealand incorporated and listed entity (A) would only be an overseas person where overseas persons:</p> <ul style="list-style-type: none"> <li>• have 50% or more of A’s total equity securities (that is, across any class of equity securities) (the ownership limb); or</li> <li>• with holdings of 10% or more of any class of A’s equity securities collectively have: <ul style="list-style-type: none"> <li>○ the power to control the composition of 50% or more of A’s governing body; or</li> <li>○ the right to exercise or control the exercise of more than 25% of the voting power at a meeting of A (the control limb).</li> </ul> </li> </ul> <p style="text-align: right;"><i>agree/disagree</i></p>		
<p>Existing exemptions for portfolio investors and New Zealand controlled entities cannot be used. This is because, following the 2018 changes to the Act, these exemptions are unlikely to meet the statutory exemption criteria.</p>	<p>Allow New Zealand incorporated companies that are majority owned and controlled by New Zealanders to apply for an exemption from the definition of overseas person.</p> <p>A domestically incorporated (but unlisted) entity (A) could apply for an exemption from the definition of overseas person provided that overseas persons:</p> <ul style="list-style-type: none"> <li>• do not have 50% or more of A’s total equity securities;</li> <li>• with holdings of 10% or more of any class of A’s equity securities, do not collectively have: <ul style="list-style-type: none"> <li>○ the power to control the composition of 50% or more of A’s governing body; or</li> <li>○ the right to exercise or control the exercise of more than 25% of the voting power at a meeting of A; and</li> </ul> </li> <li>• that are foreign governments (or their associates) do not hold 10% or more of A’s securities.</li> </ul> <p>Before granting an exemption, the Minister would be required to consider the entity’s compliance with the law and where relevant, the degree of control that a foreign government or its associates has in the entity.</p> <p style="text-align: right;"><i>agree/disagree</i></p>		

<b>Problem</b>	<b>Recommended option</b>	<b>Alternative option</b>	<b>Minister comment</b>
	<p>Allow managed investment schemes that are majority owned and controlled by New Zealanders to apply for an exemption from the definition of overseas person.</p> <p>A managed investment scheme would be eligible for an exemption from the definition of overseas person if:</p> <ul style="list-style-type: none"> <li>• more than 50% of the scheme's funds are invested on behalf of non-overseas persons;</li> <li>• overseas persons that each hold 10% or more of voting power do not collectively control more than 25% of voting power at a meeting of scheme participants; and</li> <li>• less than 10% of the scheme's funds are invested on behalf of a foreign government (alone or with its associates).</li> </ul> <p>Before granting an exemption, the Minister would be required to consider the scheme's compliance with the law and where relevant, the degree of control that a foreign government or its associates has in the scheme.</p> <p style="text-align: right;"><i>agree/disagree</i></p>		
	<p>Note that new exemptions for entities that are majority owned and controlled by New Zealanders will require an amendment to the statutory exemption criteria.</p> <p style="text-align: right;"><i>noted</i></p>		
Retirement schemes are exempt from consent requirements but are not exempt from the definition of overseas person. This means that investments by retirement schemes in a New Zealand entity (A) can result in A becoming an overseas person (and therefore requiring consent to purchase sensitive assets), even though the underlying investors in the retirement scheme are New Zealanders.	<p>Amended class exemption for retirement schemes, exempting them from the definition of overseas person rather than from consent requirements.</p> <p style="text-align: right;"><i>agree/disagree</i></p>		
	<p>Note that we do not recommend a general exemption for portfolio investors. The recommended exemptions for managed investment schemes and retirement schemes, together with changes to the tipping point below, are sufficient to address concerns relating to portfolio investors.</p> <p style="text-align: right;"><i>noted</i></p>		

<b>Problem</b>	<b>Recommended option</b>	<b>Alternative option</b>	<b>Minister comment</b>
<b>Excluding transactions that do not cross control limits [6.4]</b>			
Note that this package of reforms is designed to work coherently to address the identified problems. If you have concerns with any aspect of the package and wish to consider alternative options, we will need to provide further advice on how changes to one element might affect the package as a whole.			
	<i>noted</i>		
Overseas persons require consent for incremental investments. Some small changes in shareholdings do not require consent due to exemptions in the regulations. More generally, however, requiring investors to obtain consent to increase their shareholding, even if their level of control over sensitive assets does not change, is disproportionate to the risks being managed.	<p>Only require consent if overseas persons increase their holding in a sensitive asset above a control limit (that is, 25, 50, 75 or 100%).</p> <p>Remove existing exemption for incremental investments in regulation 38.</p> <p style="text-align: right;"><i>agree/disagree</i></p> <p>[1, 36]</p> <p style="text-align: right;"><i>noted</i></p>	<p>As per the recommended option, but retain regulation 38(2)(c)(i), so that an overseas person may increase an investment by 5% of the interest that overseas person has consent to hold irrespective of whether this results in their holdings exceeding a control limit.</p> <p style="text-align: right;"><i>agree/disagree</i></p> <p>[1, 36]</p> <p style="text-align: right;"><i>noted</i></p>	
Overseas persons require consent if their acquisition results in the target entity becoming an overseas person, even if they have no ability to exert control over a sensitive asset. Requiring consent in such circumstances is disproportionate to the risks being managed.	<p>Only require overseas persons to get consent to invest in New Zealand incorporated and listed bodies corporate if the investment results in the target entity breaching the control limb of the definition of overseas person.</p> <p style="text-align: right;"><i>agree/disagree</i></p>		

## Purpose of the report

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1. In April 2019, Cabinet invited you to report back in October 2019 to the Cabinet Economic Development Committee (DEV) on the outcomes of consultation and proposals for the second phase (Phase 2) of the Government's reforms to the Overseas Investment Act 2005 (the Act).
2. This report recommends proposals to take to DEV in October and seeks your decisions on the detailed design of the reform package. It is arranged into six sections:
  - Section 1: Background
  - Section 2: Issues with the Act
  - Section 3: Overview of proposals to simplify and improve the Act
  - Section 4: Proposals to improve the consenting framework (how we screen)
  - Section 5: Proposals to strengthen the criteria for consent (how we screen)
  - Section 6: Proposals to reduce the screening of lower risk investments (who and what we screen)
3. You are meeting with us on 8 August 2019 to discuss this advice. We recommend that you also discuss reform options with relevant ministerial colleagues (e.g. decision-making ministers under the Act). You are meeting with the Minister for Land Information and Assistant Minister of Finance (Hon. David Clark) on 22 August 2019.
4. This report does not address:
  - a whether the ministerial directive relating to rural land should be enshrined in the Act (we will discuss this further when we meet with you on 8 August);
  - b the offer back of special land to the Crown;
  - c the proposal to introduce a national security and public order call-in power;
  - d the Overseas Investment Office's enforcement powers (including the enforcement powers required to operationalise the call-in power); or
  - e the role of judicial review in relation to proposals to introduce a national interest test and call-in power.
5. We will provide advice on these issues later this month. Your decisions on these issues will be reflected in the full package of reform provided to Cabinet.

## Section 1: Background

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6. In October 2018, Cabinet agreed to Terms of Reference for reforms to the Overseas Investment Act 2005 (the Act) [CAB-18-MIN-0481 refers]. This is Phase 2 of the Government's reforms to the Act, following changes in 2018 to rationalise the screening regime for forestry assets and certain other profits-à-prendre and generally require overseas persons to obtain consent to acquire residential land (Phase 1).

### **Scope of reforms**

7. Phase 2 is considering broader changes to the Act than were enacted in Phase 1. This reflects that the Act overreaches in many circumstances, unnecessarily increasing regulatory burden and disincentivising investment that New Zealand needs. There are also some significant gaps in the Act that limit the government's ability to manage the risks of overseas investment. Phase 2's aim, having regard to the Act's purpose,<sup>1</sup> is therefore to:
- enable the Government to effectively manage overseas investment; while
  - ensuring that the Act operates efficiently and effectively; and
  - supporting overseas investment in productive assets.
8. Phase 2 does not revisit substantive issues addressed in Phase 1 (e.g. requiring purchases of residential land and forestry rights over sensitive land by overseas persons to be screened).

### **Role of the Overseas Investment Act**

9. The Act acknowledges that it is a privilege for overseas persons to own or control sensitive New Zealand assets. Overseas persons must get consent to own or control such assets, which include certain types of land, significant business assets (generally those worth at least \$100 million) and fishing quota. The majority of overseas investment in New Zealand does not require consent.
10. The Act focuses on the ownership or control of sensitive New Zealand assets by overseas persons, not their use. Other legislation regulates the activities of all persons operating in New Zealand (e.g. the Resource Management Act 1991 regulates the impact of their activities on the management of New Zealand's natural and physical resources).

#### **Applications for sensitive land and significant business assets under the Overseas Investment Act**

- **Average of 153 applications considered each year.**
- **Most applications involve sensitive land** – 70% involve sensitive land, 16% significant business assets, and 13% sensitive land and significant business assets.
- **Most applications are approved** – 90% approved, 9% withdrawn, 1% declined.
- **Application fees are up to \$54,000.**

*Data from June 2013 to August 2018*

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<sup>1</sup> "That it is a privilege for overseas persons to own or control sensitive New Zealand assets."

## Section 2: Consultation underscored the extent of problems with the Act

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11. Sustainable economic growth requires capital and New Zealand's domestic savings are insufficient to meet investment needs. Overseas investment can help bridge this gap, while also increasing productivity and wages, and supporting innovation.
12. However, overseas investment can also have risks. These include that overseas investment can take ownership and control of, and profits<sup>2</sup> from, economic activity out of New Zealand. In rare cases, this could lead to underinvestment, or firms moving offshore. High levels of foreign ownership or control of sensitive New Zealand assets can conflict with some people's view that New Zealanders should own or control those assets.
13. An effective overseas investment regime should achieve a balance between supporting high-quality investment and ensuring governments have the flexibility to manage any risk arising from overseas investment. However, while New Zealand ranks as one of the world's easiest countries to do business, there is evidence that the Act's complexity and breadth is discouraging the overseas investment that New Zealand needs. New Zealand's screening regime is restrictive by international standards.<sup>3</sup> This compounds other factors that limit New Zealand's investment attractiveness, including greater competition for investment, New Zealand's small size, and distance from markets. New Zealand consistently underperforms relative to other small states in attracting overseas investment.<sup>4</sup>
14. In April and May 2019, Treasury engaged publicly on options for reform. This included 19 meetings (with approximately 175 attendees), including five hui with representatives from iwi organisations and Māori businesses, and 733 written submissions. We provided you with advice on submitters' feedback in June 2018 [T2019/1690 refers].
15. Stakeholders underscored the extent of problems with the Act. Many users of the Act noted that applying for consent routinely costs more than \$100,000 (excluding OIO fees) and that processing times are much longer than in other jurisdictions. We heard from a number of stakeholders that this is leading to investors carving New Zealand assets out of global transactions, resulting in those assets having reduced access to capital, which may depress economic growth.
16. On the other hand, we heard concerns that the Act does not reflect important underlying values, particularly in relation to water and environmental sustainability more broadly. There is also concern that the Act does not allow decision-makers to holistically assess whether proposed investments are in the national interest. Māori stakeholders were generally keen to see more engagement with iwi and hapū, to ensure decisions take appropriate account of the impacts on Māori.
17. This feedback reflects the tensions this review is trying to manage.

### ***The Act's consent framework is complex and creates uncertainty***

18. The Act's consent framework includes the 'investor test' and the 'benefit to New Zealand test' (*the benefits test*). These tests seek to ensure investment will be beneficial, but are the primary drivers of the Act's complexity and cost.
  - a *The investor test* applies to almost all transactions. It assesses an overseas person's fitness to invest, but it does so in an inefficient and ineffective way. We agree with

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<sup>2</sup> The extent to which this is a problem is not clear – an asset's sale price should reflect the value of expected future profits, and this capital (released in the sale) may be reinvested in the New Zealand economy.

<sup>3</sup> Mistura, F. and Roulet, R. (2019). The Determinants of Foreign Direct Investment: Do statutory restrictions matter? (01/19). OECD Working Paper on International Investment.

<sup>4</sup> Mistura, F. and Roulet, R. (2019). The Determinants of Foreign Direct Investment: Do statutory restrictions matter? (01/19). OECD Working Paper on International Investment.

feedback received during consultation that the test creates uncertainty and imposes compliance costs disproportionate to the risks it manages.

- b *The benefits test* applies to most transactions involving sensitive land (and in a modified way, fishing quota) and assesses whether investment in that land is likely to benefit New Zealand. We agree with feedback received during consultation that it is unclear and unnecessarily complex.

*Requirements for consent by sensitive asset type (parts of the consent framework in scope of this review in **bold**)*

<i>Asset sensitive type</i>	<i>Consent requirements</i>
Significant business assets	<b>Investor test</b>
Residential and lifestyle land (to live in)	Commitment to reside in New Zealand
Residential and lifestyle land (not to live in)	<b>Investor test</b> , and one of four tests: increased housing test, non-residential use test, incidental use test, or the <b>benefits test</b> . <sup>5</sup>
Sensitive land that is not residential	<b>Investor test, benefits test.</b>
Forestry activities on sensitive land	<b>Investor test</b> , and one of three tests: special forestry test, modified benefits test, or the <b>benefits test</b> .
Fishing quota	Fisheries Act 1996 requirements, which link to the <b>investor test</b> and the <b>benefits test</b> .

- 19. The lack of clear timeframes further increases uncertainty for investors. This contrasts with comparable regimes in other jurisdictions, such as Canada and Australia which have statutory deadlines. OIO data suggests it takes an average of 100 days to decide an application. Many stakeholders considered timeframes to be the Act’s most serious issue.

***There are gaps in the screening regime***

- 20. Despite its complexity and expansive scope by international standards, the Act’s consent framework has clear gaps. The Act seeks to ensure that overseas investment is likely to benefit New Zealand, but does not allow decision-makers to assess investments’ likely effects holistically. These gaps limit the government’s ability to decline investments that might negatively affect New Zealanders’ wellbeing.
- 21. Of particular concern is the fact that there is limited capacity to consider a proposed investment’s implications for New Zealand’s national security or public order. This is unique among screening regimes globally. There is also no ability to consider whether an investment in a significant business asset, such as an electricity generator, is in New Zealand’s interest, even if it is a part of our critical infrastructure. Some also consider the Act should have a broader ability to consider a proposed investment’s impact on water quality and sustainability or Māori cultural values.
- 22. Finally, the Act is also unable to screen investments in business assets below the relevant monetary thresholds, or in land not classified as sensitive, even where these may present high levels of risk (for example, foreign state acquisition of sensitive technology).<sup>6</sup>

<sup>5</sup> Overseas persons can purchase an apartment off the plans in a development with an exemption certificate without obtaining consent. They cannot live in them.

<sup>6</sup> This is addressed by the proposal to introduce a national security and public order call-in power. We will provide further advice on this proposal later this month.

***Lower risk investments can be subject to screening***

23. The Act compounds costs associated with the consent framework's complexity by screening transactions that are not likely to be high risk, or relate to land unlikely to have significant ownership value to New Zealanders. Examples include:
- a requiring consent to purchase or lease land adjoining land with sensitive characteristics ("sensitive adjoining land");
  - b screening medium-term leases;
  - c treating entities incorporated in New Zealand and majority owned and controlled by New Zealanders (including entities partially owned by the Crown) as overseas persons, thereby requiring them to obtain consent to purchase sensitive assets; and
  - d imposing consent requirements on investors marginally increasing their interests in sensitive assets, even where their level of control does not change.
24. The Act's overreach in these circumstances creates unnecessary costs and delays for investors and harms New Zealand's reputation as an investment destination.

## Section 3: Overview of proposals to simplify and improve the Act

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25. This section:
- a provides an overview of the recommended package and alternative options;
  - b assesses the recommended package and alternative options against the review's criteria;
  - c indicates the potential impact of the recommended package on the decision-making process; and
  - d outlines the impact of New Zealand's international agreements on reform options (including where options are potentially constrained by these agreements).

### **Recommended reform package**

26. The recommended package includes:
- a **proposals to improve the consenting framework** – these are the tests used to establish whether a prospective investment is likely to benefit New Zealand;
  - b **proposals to strengthen the criteria for consent** – this includes changes to the benefits test to allow an investment's effect on New Zealand's tax revenue, water extraction, or Māori cultural values to be assessed;
  - c **proposals to reduce the screening of lower risk transactions** – this removes certain transactions from the regime where screening is not necessary to enable the Government to manage the risk of overseas investment.
27. To finalise these proposals, we considered all options in the consultation document and feedback from submitters. The table below sets out the recommended package, and alternative options.
28. The recommended package provides a cohesive set of reforms. The alternative options presented for most issues could be adopted in place of specific recommended options. However, for some issues there are interdependencies between specific topics or sub-topics, requiring consideration as a package. This includes options to improve the consenting framework and the recommended changes to reduce the number of low risk transactions and entities screened. We have indicated where, if you wish to explore alternative combinations of reforms, we will need to provide additional advice about impacts across the package as a whole.
29. Finally, the proposed reforms affect every part of the Act. It will be important to allow reasonable time for implementation (both to operationalise the changes and to provide certainty to applicants), before amendments come into force. Once you indicate your preferred package of reform, we will work with Land Information New Zealand (LINZ) and other agencies to identify a reasonable implementation period.

Recommended package	Alternative options
<i>Proposals to improve the consenting framework</i>	
<p>A narrowed and simplified investor test</p> <p>A simplified benefits test (positively framed), reducing the number of factors without shrinking coverage, plus:</p> <ul style="list-style-type: none"> <li>• simplify the counterfactual (applications assessed against current state of the land);</li> <li>• replace the “substantial and identifiable” benefit requirement with a requirement that the benefit be proportional to the asset; and</li> <li>• introduce a “backstop” national interest test for high-risk investment.</li> </ul> <p>Statutory deadline for applications to be processed, tailored to application type.</p>	<p>More discretion in the investor test relative to the recommended package (though less than the status quo).</p> <p>Simplified benefits test, reducing the number of factors without shrinking coverage, negative impacts considered for specific factors, plus:</p> <ul style="list-style-type: none"> <li>• simplify counterfactual (applications assessed against continued vendor ownership); and</li> <li>• introduce of a “backstop” national interest test for high-risk investment.</li> </ul> <p>No statutory timeframes (status quo).</p>
<i>Proposals to strengthen the criteria for consent</i>	
<p>Allow recognition of protections and provision for wāhi tupuna, Māori reservations, and public access by Māori for cultural purposes within the benefits test.</p> <p>Remove the farm land advertising requirements.</p>	<p>Allow recognition of protections and provision for wāhi tupuna, Māori reservations, and public access by Māori for cultural purposes within the benefits test.</p> <p>Allow water extraction and effect on tax revenue to be assessed as part of the benefits test.</p> <p>Clarify and strengthen the farm land advertising requirements.</p>
<i>Proposals to reduce the screening of lower risk transactions</i>	
<p><i>Reducing what we screen:</i></p> <ul style="list-style-type: none"> <li>• Reduce screening of sensitive adjoining land to land adjoining foreshore, lakebeds and land significant to Māori.</li> <li>• Raise threshold for screening non-freehold interests in land (e.g. leases and profits a prendre), other than residential land, to 15 years or more.</li> </ul> <p><i>Reducing who we screen:</i></p> <ul style="list-style-type: none"> <li>• Narrow the definition of overseas person to exclude domestically incorporated and listed bodies corporate and retirement schemes that are majority owned and controlled by New Zealanders.</li> <li>• Allow certain other New Zealand incorporated bodies corporate and managed investment schemes to apply for an exemption from the definition of overseas persons.</li> </ul>	<p><i>Reducing what we screen:</i></p> <ul style="list-style-type: none"> <li>• Small reduction in the types of land that are only sensitive because they adjoin sensitive land.</li> <li>• Raise threshold for screening non-freehold interests in land (e.g. leases and profits a prendre), other than residential land, to 10 years or more.</li> </ul>

*Reducing when we screen:*

- No longer require consent for incremental investments, unless the investment crosses a control threshold (i.e. 25, 50, 75 or 100%).
- No longer require an investor to obtain consent where its investment into a listed body corporate results in that entity becoming an overseas person, unless the investor obtains at least a 10% interest.

***Assessment of the recommended package against review criteria***

30. We have assessed reform options against three criteria to determine whether they meet the Government's objectives.
- a ***Manages the risk of overseas investment to New Zealanders' wellbeing*** – whether an option provides decision makers with the flexibility to effectively manage or protect against current and emerging risks from overseas investment to New Zealanders' wellbeing. It includes considering whether an option may create or increase opportunities for avoiding the Act.
  - b ***Supports overseas investment in productive assets*** – whether an option supports confidence in New Zealand as an attractive investment destination for productive investment. It includes considering whether an option minimises the costs involved in preparing applications and complying with consent conditions, and in administering and enforcing the regime.
  - c ***Encourages more predictable, transparent and timely outcomes*** – whether an option is consistent with the basic principles of best-practice regulation. It considers whether the option achieves its objectives in a way that makes the law more certain, predictable and transparent, and encourages timely decision-making. This criterion is important as it considers whether options will support investor and public confidence in the overseas investment regime.
31. These criteria are often in tension – for example, increasing the regime's predictability for investors, and to support productive investment, will often reduce decision makers' discretion to manage risks. Conversely, increasing decision makers' discretion will reduce predictability and investment attractiveness.
32. We have evenly weighted these criteria in our analysis. Your preferred option may vary from our recommendations should you prefer to weight one or more criteria more highly than others.

***Overall, the recommended package will simplify the decision-making process for most transactions and improve the Government's ability to manage high-risk investment***

33. We have thought carefully about how different parts of the recommended package interact to ensure that the Act is simpler, better manages risk, and operates coherently.

***A new consenting framework, and introducing decision-making timeframes, will have the biggest impact on the Act***

34. Proposed changes to the consent framework are the most significant part of the recommended reform package.
35. The Act's complexity and uncertainty will be significantly reduced by changes to:

- a narrow and simplify the investor test to focus on the most relevant risks to investing in New Zealand;
  - b streamline the benefits test (while maintaining the range of benefits that can be considered); and
  - c the threshold for satisfying the benefits test, to an assessment against the current use of the land rather more theoretical benchmarks that are used currently (eg. use of land by an adequately funded New Zealand purchaser).
36. These changes will in turn support overseas investment in productive assets, and encourage more predictable, transparent and timely outcomes.
37. To reflect the fact that overseas investment can pose significant risks to New Zealanders' wellbeing and to compensate for some of the simplifications, we propose a new 'backstop' national interest test to enhance the government's ability to manage risks. This test would allow holistic consideration of particularly sensitive investments, enabling Ministers to decline them if judged contrary to New Zealand's national interest (for example, if there were national security concerns). The inability to do this is a significant failing of the current regime.
38. The introduction of a 'backstop' national interest test will result in less predictable, transparent and timely outcomes for a small number of applications, but this is outweighed by the changes proposed to the other parts of the framework, which significantly improve the process for most applications by narrowing and simplifying the consent criteria.
39. The introduction of statutory timeframes will significantly improve the predictability of the application process and will require operational changes to how Ministers and the OIO assess applications and manage their workloads. Critically, however, they will also create incentives for applicants to improve application quality, reducing the OIO's workload. While the changes to simplify the consent framework should offset some of the resourcing demands related to timeframes, there may need to be an increase in OIO resourcing to meet those timeframes.

*Strengthening some consent criteria will make minor improvements to government's ability to manage the risk of overseas investment*

40. Allowing greater consideration of Māori cultural values will improve government's ability to manage risk and ensure that overseas investment in sensitive assets is consistent with New Zealanders' values. Removing the farm land advertising requirements will reduce complexity, and encourage more predictable, transparent and timely outcomes. Options to clarify and improve special land (advice on this issue is still being developed but your decisions will be reflected in package of reform provided to Cabinet) will also have a positive impact on all three criteria.
41. When considering the Government's ability to manage the risk of overseas investment, we have placed significant weight on the existence of other domestic regulatory regimes. We have therefore recommended that it is not necessary for the Act to require additional consideration of the effects of water extraction and on tax revenue.

*The proposals to reduce the screening of lower risk transactions will support overseas investment in productive assets*

42. A significant number of changes aim to reduce overreach and remove low risk transactions from screening. This includes changes to remove a number of New Zealand entities from the regime, remove land of limited sensitivity from the regime, and no longer screen transactions that do not increase an overseas persons' level of control. This will reduce the number of transactions captured by the Act and focus the regime on higher risk transactions, and thereby support high quality overseas investment and result in more predictable, transparent and timely outcomes. Removing screening where the entities

involved are effectively New Zealand-entities or the transaction does not increase an overseas persons control over sensitive assets will not reduce the government's ability to manage risk.

43. Similarly, changes to reduce the amount of land screened only because it adjoins sensitive land and/or is a short-term interest in land will only marginally reduce the government's ability to manage the risks of overseas investment. This is because the risks associated with the purchase of sensitive adjoining land are not specific to overseas investment, and for short-term interests in land, the ownership of the underlying asset does not change (and control of the asset is time-limited).

***The alternative options offer an increased ability to manage risk but add complexity and uncertainty to the regime***

44. The alternative options offer trade-offs compared to the recommended package in that they generally improve the government's ability to manage risks, but add complexity and uncertainty to the regime. If you choose *all* the alternative options as a package and/or retain elements of the current regime, there is a risk that any changes that increase New Zealand's attractiveness to productive investment will be offset by this increased complexity and uncertainty.
45. One of the most significant choices is whether to enable Ministers to consider negative effects for some factors under the benefits test. This will improve the government's ability to manage risks, but significantly reduce predictably and risks undermining the Act's coherency. The net impact of enabling consideration of negative effects, if combined with the "backstop" national interest test, would be to introduce considerably more complexity and uncertainty to the regime relative to the status quo.
46. Adding factors to the benefits test also risks sending a negative signal about New Zealand's openness to investment, and introducing further complexity and uncertainty to the benefits test, in particular:
- a enabling the benefits test to consider tax revenue would increase compliance and administrative costs for most applications, given the significant complexities in assessing tax arrangements; and
  - b considering the effects of water extraction would introduce complexity to the benefits test, but at best only marginally improve the Government's ability to manage risks.
47. The alternative options to reduce the screening of lower risk leases and sensitive adjoining land will only marginally improve the Government's ability to manage risks relative to the recommended package.

***The Government's strategic approach to overseas investment***

48. Investments receive consent if they are beneficial to New Zealand. The Act provides a neutral and enduring framework for Ministers to determine whether an investment meets the criteria for consent on a case-by-case basis. Within this framework, the Government can outline its policy approach towards overseas investment through a Ministerial directive letter.
49. We have explored whether the Act should explicitly enable the Government to produce a Government Policy Statement (GPS) on overseas investment, to help determine whether specific investments are beneficial and therefore whether consent should be granted. We do not recommend this approach as:
- a a strategic statement, such as a GPS, is unlikely to be sufficiently detailed to support decision-making at a practical level (e.g. by prioritising sectors or regions for overseas investment);

- b the Ministerial directive letter already provides some scope for the Government to outline its policy approach towards overseas investment regulated by the Act (consistent with the Act's purpose and scope), and could direct the OIO to take account of a policy statement external to the Act;
- c the Act provides space for consent decisions to align with the Government's broader economic strategy objectives, such as supporting regional growth, or a just transition to a low carbon economy; and
- d a GPS would not facilitate a comprehensive approach to managing overseas investment as it would only apply to the small proportion screened by the Act.

***International agreements constrain some of our policy choices***

50. New Zealand's international agreements limit our ability to expand our screening regime's scope. We have worked with the Ministry of Foreign Affairs and Trade (MFAT) to assess the consistency of reform proposals with those agreements.

[1, 36]

***These changes are unlikely to impact significantly on New Zealand's OECD FDI restrictiveness ranking***

53. The OECD assesses New Zealand's regime as the seventh most restrictive to foreign direct investment (FDI) out of 68 countries, including all OECD countries. This ranking largely results from the low monetary threshold for screening significant business assets, and the significant amount of land screened under the Act. The reform package will not materially alter that ranking. The OECD's methodology focuses on statutory restrictions but does not consider the implementation of those restrictions. Some changes will relax statutory restrictions (for example, the options to remove lower risk investments from screening) but the most significant changes recommended improve how those restrictions are implemented (i.e. the consenting framework) and will not affect New Zealand's ranking.

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[1, 36]

**However, OECD research suggests that any liberalisation is likely to have a positive effect on FDI inflows**

54. OECD research suggests that regardless of the methodology used to account for restrictions, more restrictive countries are less likely to receive foreign investment. Using their own methodology, the OECD's research suggests a 10% reduction in the level of restrictiveness could increase bilateral FDI stocks by around 2.1% on average.<sup>8</sup> The changes made by the reform package to relax statutory restrictions, and improve the implementation of those restrictions, should have a positive impact on FDI inflows, but quantifying this impact is difficult.

**Overseas Investment Office comment**

55. The OIO has provided the following comments on the potential impact of proposed reforms:

“Until a preferred package of policy changes is identified it is different to fully assess the resourcing and financial impact on the OIO. The OIO is undertaking a shift in how it operates as a regulator, significant work has been undertaken to improve processes and shift the culture of the OIO to improve transparency and ensure that it is well equipped to be a high performing regulator.

A number of the proposed changes will further support the OIO by providing legislative clarity and may reduce the time taken to assess in some areas of the regime. A number of the proposals will simplify the regime and provide clarity for applicants however will not necessarily reduce the scope of what the OIO needs to consider.

In some areas the preferred options will require significant changes to how the OIO operates, including an enhancement of the pre-application screening process to ensure that the OIO has all of the information required to assess the application should statutory timeframes be adopted.

A narrowing of who is captured by the regime through some of the proposals will likely reduce the number of applications processed by the OIO, so there will need to be consideration of the impact on future revenue. The impact of the national interest and national security aspects of assessment will require careful consideration of resourcing needs, particularly where volumes are difficult to determine.

LINZ is undertaking a review of the OIO Fees Regime in the 2019/20 financial year as part of the implementation of the Phase I changes to the Overseas Investment Act and the impact of Phase II changes will need to be included in this work.”

**Departmental consultation**

56. We have worked closely with relevant agencies to develop the recommended reform package. These agencies include LINZ (including the Overseas Investment Office), the Ministry of Foreign Affairs and Trade, the Ministry of Business, Innovation and Employment, Te Arawhiti, Te Puni Kōkiri (TPK), the Ministry for Primary Industries (MPI), New Zealand Trade and Enterprise, the Ministry for the Environment, the Walking Access Commission (WAC) and the Department of Conservation (DOC).
57. We are working with MPI to determine how proposed changes to the investor test and benefits test can be reflected in the Fisheries Act (in relation to overseas investment in fishing quota),<sup>9</sup> to ensure consistency across the overseas investment screening regime.

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<sup>8</sup> Mistura, F. and Roulet, R. (2019). The Determinants of Foreign Direct Investment: Do statutory restrictions matter? (01/19). OECD Working Paper on International Investment.

<sup>9</sup> The Act incorporates by reference Fisheries Act provisions relating to overseas investment in fishing quota.

58. Our recommended package reflects the need to take a broad view of how best to support overseas investment while managing its risks. Some agencies we consulted with (the DOC, MPI and the WAC) disagree with our recommended option for reducing the scope of sensitive adjoining land, suggesting that it would limit opportunities for environmental and access conditions to be imposed. MPI and the WAC note the impact on access conditions would be relatively minor. The alternative option provided reflects these concerns, by only removing the category of adjoining land generally of the least environmental, historic and cultural value and where there are rarely access concerns.
59. TPK expressed broader concerns about the scope of the review when consulted on a draft of this report. It did not raise these concerns when consulted on the Terms of Reference in September 2018. TPK's feedback suggested the review's scope should allow for adopting manaakitanga, kaitiakitanga and whanaungatanga in Act's decision-making framework, and should consider a change in the treatment of former Māori lands (particularly raupatu – confiscated land) screened by the Act, requiring them to be offered for purchase to Māori with an interest in that land before consent is granted. These issues are outside the Terms of Reference.

## Section 4: Proposals to improve the consenting framework (how we screen)

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60. This section proposes improvements to the Act's consenting framework – that is, the tests used to establish whether a prospective investment is likely to benefit New Zealand. It includes proposals to improve the investor test and the benefits test as well as a new 'backstop' power for higher risk transactions. It also recommends introducing statutory timeframes for decision-making.
61. We recommend:
- a a narrower and simplified investor test;
  - b a simplified benefits test (with no consideration of negative effects) combined with a national interest 'backstop' test;
  - c a simplified 'before and after' counterfactual test for assessing the level of benefit;
  - d a proportionality requirement in the application of the benefits test; and
  - e statutory deadlines for decision-making, tailored to each consent pathway.
62. These changes have the potential to make the biggest impact to the operation of the overseas investment screening regime. They also directly engage trade-offs between providing certainty to investors and ensuring decision-makers have sufficient flexibility to manage risk. Overall, we consider the proposed package strikes an appropriate balance between managing the risks associated with overseas investment, and improving transparency and predictability.
63. We also set out alternative reform options, which would strike a slightly different balance between these objectives. Alternative proposals include:
- a a simplified benefits test that takes account of some negative effects; and
  - b an alternative counterfactual test (considering what would happen if the vendor continued to own the land); and
  - c a 'no-detriments' test for sales between overseas persons.
64. Generally, these alternatives may emerge as the preferred package if greater weight is placed on the need to manage risk rather than on increasing predictability and New Zealand's attractiveness to investment. We have not recommended these changes as they would add significantly more complexity and create additional uncertainty for investors.

#### 4.1 How should we test an investor’s fitness to invest in New Zealand?

Option	Impact summary		
<i>Recommended option:</i> Narrower and simplified investor test, limited consideration of corporate character, limited consideration of allegations	Manages the risks of investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
	Moderately negative	Strongly positive	Strongly positive
<i>Alternative option:</i> Narrower and simplified investor test, slightly more consideration of allegations	Neutral	Moderately positive	Moderately positive

65. Overseas persons<sup>10</sup> seeking consent to invest in sensitive New Zealand assets<sup>11</sup> must, in most cases, satisfy the investor test.<sup>12</sup>
66. The investor test’s purpose is to assess overseas persons’ suitability for investing in New Zealand. That is, whether they are likely to realise the benefits of their proposed investment or pose any risks.
67. In line with this purpose, the investor test looks at four character and capability criteria:
- a whether the overseas person is of good character;
  - b whether they are eligible for a visa under sections 15 and 16 of the Immigration Act 2009 (under which visas are denied to persons with certain convictions or considered a threat to security, public order or public interest);
  - c their business experience and acumen; and
  - d their financial commitment to the investment.
68. To satisfy the investor test, overseas persons disclose and the OIO assesses information relevant to the four criteria, such as examples of offences or contraventions of the law, allegations, CVs, and evidence of due diligence costs relating to the investment in question.
69. It is more common for applications to be declined on the basis of the benefits test rather than the investor test. Where overseas persons are declined under the investor test, it is mostly because they have not satisfied the good character criterion.
70. The investor test creates considerable uncertainty and imposes compliance costs that are disproportionate to the risks being managed. This is driven by a range of factors, including:
- a no clearly stated purpose for the investor test, creating ambiguity for decision-makers and investors;
  - b broad definitions of relevant overseas person (ROPs) and individuals with control over relevant overseas persons (IWCs), resulting in uncertainty and a perception that the

<sup>10</sup> The investor test focuses on the overseas person(s) with the most influence over the proposed investment – that is, the ‘relevant overseas person’ (ROP) or, where the ROP is not a natural person, the ‘individual with control’ (IWC) over the ROP. Decision-makers determine who the relevant ROP and IWC are in respect of each transaction.

<sup>11</sup> This includes fishing quota. The investor test in respect of fishing quota is at section 57G of the Fisheries Act 1996. Any changes to the investor test in the Overseas Investment Act should be reflected in the Fisheries Act.

<sup>12</sup> Overseas persons can acquire an interest in residential land, in limited circumstances, without being required to satisfy the investor test.

test captures individuals who, in practice, have limited involvement with the prospective investments;

- c the investor test's application to New Zealanders where they are identified as ROPs/IWCs, despite their entitlement to acquire sensitive assets in their own right, without being screened;
- d the requirement for repeat investors to satisfy the investor test with every investment;
- e the breadth of the good character, financial commitment and business experience and acumen criteria; and
- f duplication between section 15 of the Immigration Act and the good character criteria.

71. A further concern is that the investor test does not allow decision-makers to consider the character of non-natural persons (e.g. corporate entities) involved in the investment (other than where corporate actions can be imputed to the character of the individual investor).
72. Submitters generally supported narrowing the investor test to ensure it only captures matters that are relevant to an overseas person's fitness to invest in New Zealand, with most preferring some kind of 'checklist' model. There was general support for the additional proposals (excluding New Zealanders<sup>13</sup>, introducing a standing consent and including consideration of corporate character).

***We recommend a new, narrowed and simplified investor test***

73. To reduce compliance costs and increase certainty, we recommend introducing a new, narrower investor test that adopts elements of the checklist model proposed in the consultation document. However, where the consultation document model proposed making the checklist factors determinative (i.e. all must be satisfied in order to satisfy the test), we recommend allowing decision-makers to have regard to and weigh the factors as they consider appropriate. This allows for more discretion than a 'bright-line' checklist.
74. We also set out an alternative option which, compared to our recommended approach, would – generally – give decision-makers even greater discretion. There is scope to adopt a package that combines elements from either option according to the preferred balance between certainty and discretion.
75. Both options recommend:
- a introducing a purpose statement in the Act that clarifies the investor test's purpose;
  - b providing additional clarification on ROP/IWC selection via operational means e.g. a Ministerial directive letter and OIO guidance (while it would be desirable to clearly define the scope of those eligible to be selected as the ROP/IWC, a bright-line definition could encourage avoidance measures so is not recommended);
  - c excluding New Zealanders who are identified as ROP/IWCs from the need to satisfy the test;
  - d introducing a 'standing consent' which would exempt individual ROP/IWCs from needing to satisfy the investor test with every investment, unless there had been changes to their character or capability (the notification of which would be mandatory);
  - e narrowing the character criterion by removing two requirements which drive significant administrative and compliance costs:

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<sup>13</sup> This also includes persons ordinarily resident in New Zealand.

- i the requirement to consider, as a reflection of individual character, contraventions and offences by or allegations against entities in which the ROP/IWC has a 25% or more ownership or control interest (e.g. an entity in which they own securities).<sup>14</sup> This requirement rarely results in negative character findings; and
  - ii removing the requirement to consider “any other matter that reflects adversely on the person’s fitness to have the particular overseas investment”;
- f narrowing the visa eligibility criterion by focusing only on security, public order and public interest matters only (section 15 of the Immigration Act). Information on offences and contraventions would be captured by other aspects of the proposed investor test; and
- g removing the financial commitment criterion, as it is of limited value to the decision-making process and no one has ever been declined on this ground.
76. Under both options, the current requirement for applicants to provide a statutory declaration attesting to their character and visa eligibility would continue, as would making remaining of suitable character a condition of consent (with enforcement action taken if this condition is not met).
77. The two options differ in their treatment of offences, contraventions, allegations and business capability. Our recommended option would, broadly, provide greater certainty for investors than the alternative.

***Narrowed character criterion: treatment of offences, contraventions and allegations***

78. Currently the good character criterion requires applicants to disclose and decision-makers to consider any actual or alleged offences or contraventions of the law. The breadth of these requirements creates considerable administration and compliance burden, as well as uncertainty for investors.
79. We recommend a narrower assessment, which:
- a is limited to offences and contraventions that are relevant to an overseas person’s suitability to invest in New Zealand, with relevance determined by seriousness, type and/or time period (for example criminal offences punishable by a term of imprisonment and civil contraventions resulting in pecuniary penalties and enforceable undertakings, in any jurisdiction)<sup>15</sup>; and
  - b narrows the consideration of allegations (for example, to those relating to relevant offences and contraventions for which official proceedings have commenced, in any jurisdiction). The national interest test could also provide a backstop to scrutinise significant risks where the overseas person was subject to relevant allegations for which there were no official proceedings.
80. These options would significantly increase certainty for investors and reduce the administrative burden on the OIO. However, if you prefer greater discretion to manage potential investor risks, our alternative option would allow decision-makers to:
- a determine the relevance of particular offences and contraventions when undertaking the assessment (with reference to the test’s purpose) – operational guidance could provide additional certainty on how relevance is determined; and

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<sup>14</sup> See Overseas Investment Act section 19(1)(a).

<sup>15</sup> Pecuniary penalties are non-criminal monetary penalties imposed by a court in civil proceedings. Enforceable undertakings are an alternative to prosecution whereby the applicant agrees to do certain things (e.g. remedy breaches) in exchange for the regulator not filing charges.

- b consider a broader set of relevant allegations (for example, those for which official proceedings or investigations have commenced).

### ***Narrowed capability criterion***

- 81. An overseas person's business capability is currently assessed through the business acumen and experience criterion, under which decision-makers consider factors such as the overseas person's CV and submissions attesting to their acumen and experience in relation to the investment under consideration.
- 82. The value of this criterion is unclear. While the OIO does see applications where the overseas person lacks the business experience and acumen necessary to make a success of the investment, we understand that this is not common. Moreover, New Zealanders are able to purchase assets without demonstrating requisite experience, with general legislation (such as the Commerce Act and the Insolvency Act) mitigating the public impact of business failure.
- 83. We therefore recommend an objective assessment in which overseas persons declare, and decision-makers consider, factors such as undischarged bankruptcies and disqualifications. This approach would focus assessment on risks associated with prior business failure or penalties.
- 84. If you prefer a more subjective test providing for a broader assessment of an overseas person's capability to deliver on the benefits of their proposed investment, we would recommend continuing the current approach of looking at applicants' CVs and submissions, as well as considering bankruptcies and disqualifications. This approach would require repeat investors (if you agree to the 'standing consent' proposal) to still demonstrate business acumen for each transaction.

### ***Additional option: considering corporate character as part of the investor test***

- 85. Currently, corporate character can only be considered indirectly under the investor test. Section 19(1)(a) requires decision-makers to consider, as a reflection of individual character, contraventions and offences by or allegations against entities in which the ROP/IWC has a 25% or more ownership or control interest. We have recommended removing this requirement as it results in considerable administrative and compliance costs yet rarely results in negative character findings against the individual investor.
- 86. As an alternative, we recommend amending the Act to explicitly allow for the consideration of corporate character. This would enable decision-makers to have regard to convictions or penalties that fall on a corporate entity rather than just the individual, which should be more efficient than the current approach of imputing corporate actions to individual directors.
- 87. However, this option could:
  - a increase administration and compliance costs, due to the additional information required (though this may be somewhat offset by removing the requirement to consider contraventions, offences or allegations relating to entities in which the ROP/IWC has a 25% or more ownership or control interest);
  - b increase uncertainty for investors (at least until decision precedent emerges);
  - c send a negative signal about New Zealand's openness to investment (we are not aware of any other investment screening regime that explicitly includes a test of corporate character, though it can be considered under some broadly cast regimes, for example through Australia's interest test).
- 88. These risks could be mitigated by:

- a prescribing the offences or contraventions to be considered (e.g. criminal offences punishable by imprisonment and civil contraventions resulting in pecuniary penalties and enforceable undertakings);
- b clearly defining the entities in scope. We recommend limiting consideration to the entity/entities that have substantive control over the investment (i.e. the parent company), as their character has the most bearing on the behaviour of the investing entity. We do not recommend capturing *all* entities within the corporate group. While this would provide decision-makers with more discretion, it would create a disproportionately large administrative and compliance burden relative to the risks posed by the wider corporate group. This would negate the efficiency gains made through other proposed changes to the investor test.

***Additional option: shifting to a post-consent model for the investor test***

89. You asked us to consider shifting the investor test from a pre-consent screening tool to a post-consent compliance and enforcement one. This would mean decision-makers would not consider an overseas investor's suitability to invest in New Zealand as part of the consent process.
90. This option could involve:
- a requiring investors to provide, as part of their application, a statutory declaration that they are and will remain suitable for investing in New Zealand (according to the test's character and capability criteria);
  - b requiring the investor to remain fit to invest as a condition of consent, and to inform the OIO if this status changes; and
  - c allowing the OIO to take appropriate enforcement action if, post-consent, it emerges (either through OIO inquiries or from information provided by the investor) that an investor no longer meets the test's criteria for investing in New Zealand.
91. This option could broadly fit with either our recommended or alternative test designs and would significantly reduce decision-making timeframes. However, it would:
- a limit the flexibility to manage risk by declining on the basis of character or capability, though in practice this may not result in significantly different outcomes as most applicants pass the current investor test;
  - b reduce investor certainty; and
  - c exclude investments in sensitive business assets from the screening regime (as these do not go through the benefits test). However, overseas investors in sensitive business assets would still need to notify the OIO and complete the statutory declaration. The proposed national interest test would provide a backstop for applications of concern involving high-risk investors.
92. This option would also reduce the administrative burden of applying the investor test. However, in cases where concerns about an investor's suitability emerge, addressing these would require greater resource than under the status quo. This is because the burden of proof would shift to the OIO to prove the investor was no longer suitable, with the evidential threshold for taking enforcement action higher than required to deny consent in the first place. For offshore directors, this approach may crystallise concerns about the proportionality of enforcement responses and the ability to enforce outside New Zealand.
93. On balance, we do not recommend this option.

## 4.2 How should benefit to New Zealand be determined?

Options	Impact summary		
<p><i>Recommended options:</i></p> <p>Simplified benefits test with national interest 'backstop' test for higher risk applications</p>	Manage the risks of investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
Replacing the current counterfactual with a 'before and after' test that compares the applicant's plans to the state of the land at the time of the application	Strongly positive	Moderately positive	Moderately negative
Introduce a legislative requirement that benefits must be proportionate to the sensitivity of the land and remove the 'substantial and identifiable' benefit threshold	Moderately negative	Moderately positive	Moderately positive
<p><i>Alternative options:</i></p> <p>Simplified benefits test with a national interest backstop (as above) with ability to consider narrow set of negative effects in benefits test</p>	Moderately positive	Neutral	Moderately positive
Simplified benefits test with a national interest backstop (as above) with ability to consider narrow set of negative effects in benefits test	Strongly positive	Neutral	Moderately negative
Replacing the current counterfactual with a comparison of the applicant's plans to continued ownership by the vendor	Neutral	Neutral	Moderately positive
Introduce a 'no detriments' test for sales between overseas persons	Moderately negative	Strongly positive	Strongly positive

94. As well as satisfying the investor test, overseas persons purchasing sensitive land and fishing quota must generally satisfy the benefit to New Zealand test (benefits test).<sup>16</sup> If the relevant land includes non-urban land of more than five hectares, the benefits must be, or likely be, substantial and identifiable.
95. In considering whether a prospective investment satisfies the benefits test, decision makers must determine this by reference to 21 economic, environmental, and cultural factors.<sup>17</sup> The number of factors, overlap between them, and ability to add to this list via Regulations creates significant compliance costs and uncertainty for investors. It also limits decision makers' ability to assess proposed transactions holistically.
96. Decision makers assess benefit against what is likely to happen if the overseas investment does not proceed (the counterfactual test). The current test is highly theoretical, particularly where the counterfactual is presumed to be a "competent and adequately funded alternative New Zealand purchaser." There is a high degree of subjectivity in determining the appropriate counterfactual. There are also difficulties in demonstrating incremental benefit in sales between overseas persons, where the assets are large and well-managed or mature. This can result in the asset's owners being unable to exit an investment where there is no alternative New Zealand buyer and therefore unable to reinvest that capital into New Zealand (the 'stranded assets' problem).

<sup>16</sup> Different tests can apply to the purchase of residential land or sensitive land to be used for forestry activities.

<sup>17</sup> In respect of fishing quota, some additional criteria are specified in section 57H(2) of the Fisheries Act 1996.

97. The higher “substantial and identifiable” threshold recognises the special ownership value attached to non-urban land greater than five hectares, but introduces additional uncertainty and may not be necessary as the OIO applies a proportionate approach to decision making.
98. In addition, and despite the large number of factors, the Act does not allow decision makers to consider national security risks (or other significant risks, e.g., to public order) associated with a proposed investment.<sup>18</sup> There is also general uncertainty about whether negative effects (that is, any downsides of the investment) can be considered under the current test.
99. To address these issues we consulted on options to:
- a reform the benefits test (including options to expand and/or simplify the test’s factors, introduce a ‘backstop’ test for high risk applications, or replace the benefits test with a national interest test);
  - b simplify the counterfactual test, including introducing a ‘no detriments’ test for sales between overseas persons to address the risk of assets becoming stranded; and
  - c remove the “substantial and identifiable” benefit threshold.
100. We also consulted on an option to introduce a ‘call in’ power that could be used to screen investments not ordinarily subject to the Act (such as business assets worth less than \$100 million) where these present risks to New Zealand’s national security and/or public order. We are providing additional advice on the ‘call in’ power later this month.

### ***Stakeholders support changes to the benefits test***

101. The benefits test is a primary driver of the time and cost involved in obtaining consent. There was little support among submitters for retaining or expanding the current test.
102. Most submitters (largely legal advisers and investors) supported a new simplified benefits test that retains the current range of benefits, with a ‘backstop’ test for higher risk transactions.<sup>19</sup> Most did not support an explicit ability for decision-makers to consider negative impacts, on the grounds it would exacerbate current issues with the complexity, uncertainty and cost, particularly as it would be hard for decision-makers to make a trade-off between different factors. Some submitters suggested that any ‘backstop’ test be framed negatively (that is, investments could only be blocked if they were found to be contrary to New Zealand’s national interest).
103. Submitters also generally supported replacing the counterfactual test with a ‘before and after’ test that would compare an overseas person’s plans with the state of the land, and activities on the land, at the time the application is lodged. This would remove the test’s hypothetical component - a major contributor to the time and cost involved in obtaining consent.
104. There was general support for a no-detriments test for sales between overseas persons. This would require a prospective overseas buyer to demonstrate that they would at least maintain the benefits associated with the vendor’s continued ownership of the land. This was seen as particularly useful to facilitate the sale of well-managed assets between overseas persons.

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<sup>18</sup> While an investor that posed a national security risk could be denied consent under the investor test, there is no ability to decline where it is the investment (rather than the investor) that poses a risk to national security. This is out of step with comparable regimes globally (including Australia, the United States, Canada, Germany, France and Japan).

<sup>19</sup> That is, a national interest test or a substantial harm test.

105. Submitters overwhelmingly supported removing the “substantial and identifiable” threshold (though many endorsed proportionate and risk-based decision-making). Some gave anecdotal examples of the test leading to under investment by existing owners to better enable a future purchaser to demonstrate substantial benefit.
106. We discuss our proposed reforms to the benefits test, the counterfactual test, and the “substantial and identifiable” threshold below.

#### **4.2.1 Recommended option: a simplified benefits test coupled with a ‘backstop’ national interest test**

107. Our preferred approach includes a:
- a simplified benefits test with broadened economic, environmental and access factors (but no reduction in the scope of benefits that can be considered relative to the status quo), with no ability to take account of negative effects. Factors could no longer be added through regulations, and
  - b new, national interest ‘backstop’ test, enabling Ministers to decline higher risk transactions that are contrary to New Zealand’s national interest.

#### ***Recommended option: a simplified benefits test including broad economic, environmental and access factors, with no negative weighting of factors***

108. A simplified benefits test would:
- a include a broadly framed economic benefit factor, supported by a non-exhaustive list of illustrative types of benefits that could be considered (e.g., new technologies or skills, increased exports, increased competition, and any reduction in the risk of assets being stranded);
  - b include a broadly framed environmental factor, supported by a non-exhaustive illustrative list of benefits (e.g., conservation benefits);
  - c include a general public access factor (to replace the existing narrower walking access factor);
  - d maintain a factor relating to historic heritage;
  - e maintain a factor relating to advancing significant Government policies;
  - f maintain a factor relating to levels of New Zealanders’ involvement in the overseas investment and any relevant overseas person; and
  - g maintain a factor relating to the extent to which the investment will, or is likely to, result in any other benefit (i.e. consequential benefits).
109. We will provide further advice on the potential inclusion of the offer back of special land to the Crown in a simplified benefits test.
110. These changes seek to maintain the scope of the benefits test and the government’s ability to manage risk, while improving investor certainty and reducing the test’s regulatory burden. In particular, the broadly framed economic, environmental and public access factors should enable a simpler and more transparent demonstration of benefits, including benefits against these factors that currently have to be listed against the ‘consequential benefits’ factor. This benefits focussed test could also be expanded to include factors relating to water, tax, and/or Māori cultural values, depending on your decisions on Section 5 of this report.

111. We do not recommend enabling decision makers to consider negative effects as part of the simplified benefits test, because:
- a the new national interest backstop test will manage significant risks; and
  - b general legislation (for example, the RMA and the Commerce Act), and sometimes the counterfactual, can manage lower order risks. The counterfactual could have this effect because an application that would produce outcomes in relation to a particular factor that were poorer than those already resulting from the land would not satisfy that element of the counterfactual test.
112. In addition, an ability to negatively weight factors would make screening less predictable (because it would involve trade-offs between very different factors), more costly and time-consuming (with the OIO noting a likely need for additional capacity and more information from applicants), and would duplicate existing legislation.
113. We recommend removing the ability to add factors to the benefits test by regulation, as this undermines investor certainty and enables the government's executive branch to make significant policy choices that are more appropriately considered by Parliament.

***Alternative option: benefits test includes a narrow set of negative effects***

114. An alternative option would mirror the preferred approach, but allow Ministers to consider any negative effects of an investment against a limited range of factors, and balance these against their assessment of benefits before deciding whether to grant consent. Given the time, cost and potential duplication involved in considering negative effects (as noted in the section above), we recommend limiting any consideration of negative effects to factors with particularly high cultural value or where there are perceived gaps in existing legislation – for example, access factors. If you decide that the test should include factors relating to water and tax, negative effects relating to these factors could also be considered as a part of the benefits test (discussed further below).
115. This option would marginally improve the ability to manage the risks of overseas investment (e.g., for investments that do not meet the threshold for the proposed national interest test). It could also assist in ensuring that the 'back stop' test remains a reserve power only (rather than being used as an adjunct to the benefits test). It would have a moderately negative impact on predictability and transparency and impose an additional compliance burden, reducing New Zealand's attractiveness to overseas investment. The OIO advise that it would materially increase their workload and increase processing times.

***Recommended option: introduce a 'backstop' national interest test focussed on managing risks***

116. We recommend a national interest test to serve as a 'backstop' to the simplified benefits test and investor test. This is a necessary to ensure the Act provides scope to manage significant risks to New Zealand – particularly public order and national security risks.
117. We therefore recommend that Ministers be able to consider higher risk transactions – in any category of asset screened under the Act – and decline those that are contrary to New Zealand's national interest. It would apply in addition to the tests ordinarily required to obtain consent (the investor test and the benefits test) and is the only part of the recommended consent framework that will allow Ministers to account for any risks posed by the investment (rather than the investor).
118. The national interest test would enhance the government's ability to manage significant risks associated with overseas investment (whether they relate to the investor or the investment). While it would create some additional uncertainty and increase costs for

high-risk investments, the overall reform package (including the simplified investor and benefits tests) is likely to result in cost and time savings for the majority of applications.

119. To ensure the national interest test operates transparently, and to mitigate uncertainty, we recommend:

- a that the national interest test is negatively framed;
- b prescribing criteria to be considered before an application can be declined;
- c prescribing classes of transactions that will always be subject to the 'national interest' test, with other transactions to be considered on a case-by-case basis;
- d allocating decision making responsibility under the national interest test to a Minister other than the Minister ordinarily responsible for decision making under the Act; and
- e requiring public notification of decisions to decline on national interest grounds, with reasons (unless this is not possible for national security reasons).

120. These are discussed below.

### ***Test should be focused on managing risks***

121. We consulted on a backstop national interest test focussed on assessing the prospective benefits of a particularly sensitive transaction (i.e. an applicant would need to demonstrate that its investment is in the national interest – a 'positively' framed test). On reflection, we do not recommend a positively framed test because it would:

- a duplicate the requirements of the simplified benefits test, reducing the Act's coherency;
- b impose significant and unnecessary costs on applicants and decision makers because of the amount of information and analysis that would be required to demonstrate that an application was in the national interest;<sup>[2]</sup> and
- c go further than a true 'reserve power' designed to manage significant risks. This is because the test would remain focussed on identifying benefits, rather than reducing potential significant harms to New Zealanders.

122. Accordingly, we recommend a 'negatively' framed national interest test, focussed on risk. That is, the government could deny consent if an investment was contrary to the national interest.

### ***Decision-making criteria under national interest test***

123. In considering whether an investment is contrary to New Zealand's national interest, we propose that the Minister be required to have regard to:

- a the outcome of the benefits test (above), and any other benefits rising from the transaction;
- b any significant risks to national security, public order, international relations, the economy, the environment, or other national interests;
- c the extent to which any of these risks to New Zealand's national interests can be mitigated by conditions of consent; and

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[2]

d any other matters the Minister considers relevant.

124. We propose all decisions would need to be made consistent with New Zealand's international obligations. This is an important signal for our international partners and consistent with what is proposed for the design of the 'call in' power.
125. These criteria are intended to provide clarity for investors and courts around the test's intended scope and operation. They would be subject to further refinement during the legislative drafting process.
126. The Government could also issue guidance on the types of factors that are likely to give rise to national interest concerns. This guidance would not limit the Government's ability to consider each application on a case-by-case basis, but would provide investors with a sense of each Government's priorities and interests in respect of foreign investment.

### ***Transactions subject to the national interest test***

127. We recommend the national interest test be a 'backstop' power, rarely used and only in relation to high risk transactions. To provide certainty to investors, we recommend that certain classes of investment (whether screened because they involve sensitive land or significant business assets) always be subject to the test, including:
  - a investments where a foreign government or its associates have a 10% or greater interest in the relevant asset (given the risk that government investors have strategic, rather than commercial objectives);
  - b investments identified by the New Zealand security agencies (that is, the GSCB and the NZSIS) as posing a material risk to national security; and
  - c investments in strategically important industries and entities and high-risk critical national infrastructure (broadly those most important to the day-to-day wellbeing of New Zealanders). That is:
    - i significant ports and airports;
    - ii electricity generation and distribution businesses;
    - iii water infrastructure;
    - iv telecommunications infrastructure;
    - v certain media entities;
    - vi entities with access to, or control over, dual-use or military technology;
    - vii critical direct suppliers to the New Zealand Defence Force or security agencies; and
    - viii systemically important financial institutions and market infrastructure (e.g., payments systems).<sup>21</sup>
128. These categories of investment could be prescribed in either primary or secondary legislation.

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<sup>21</sup> We are working with MBIE, Ministry of Transport and the RBNZ to refine these classes of investment. The categories largely mirror the types of assets proposed to be covered by the national security 'call in' power, with the exception of entities holding 'sensitive data', consistent with advice provided to you in July 2019 [T2019/1394 refers].

129. Other transactions posing significant risk to New Zealand could be assessed on a case-by-case basis and referred to the relevant Minister to determine whether the application should be subject to the national interest test. This could include, for example, investments in entities:
- a with access to sensitive data (given their proposed coverage under the ‘call in’ power), and
  - b that would result in a significant portion of an industry or supply chain being owned by a limited number of entities.

### ***Decision-making responsibility under the national interest test***

130. We propose that decisions under the national interest test be taken by a Minister other than the Minister ordinarily responsible for assessing the particular application. For example, the Minister of Finance could take decisions under the ‘national interest’ test where an Associate Minister of Finance ordinarily makes decisions on applications to acquire significant business assets.<sup>22</sup> This power could not be delegated to the OIO.
131. Separating responsibility for the national interest test from the Act’s other tests creates a degree of independence and reflects that this is a reserve power to be exercised only in exceptional circumstances.

### ***Public notification and review of decisions under the national interest test***

132. We recommend that decisions to decline an application under the national interest test are publicly notified with reasons given for the decision (unless the decision or aspects of the decision must remain confidential to protect national security, New Zealand’s international relations, or to protect commercial-in-confidence information).
133. Decisions under the national interest test could be judicially reviewed, or reviewed through an alternative mechanism, in either case with appropriate protection for national security information. We will provide advice on review mechanisms in relation to both the national interest test and the proposed ‘call in’ power later this month.

### ***Options not assessed***

134. Following public consultation <sup>[1]</sup> we have not progressed options to:
- a expand the benefit to New Zealand test with an ability for decision-makers to consider negative effects in relation to all the factors in the benefits test;
  - b have a simplified net benefit to New Zealand test where decision-makers can consider negative effects in relation to all factors, coupled with either a ‘substantial harm’ or ‘national interest’ backstop; or
  - c replace the benefit to New Zealand test with a ‘national interest’ test that applies to all applications screened under the Act.
135. These models would significantly increase the Act’s compliance burden on investors (most, if not all, applicants would be required to provide additional information on the potential negative effects of their investment), increase processing times, and increase the administrative burden across government. As above, any consideration of negative effects would also introduce issues in weighing the pros and cons of different types of factors against each other.

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<sup>22</sup> This is consistent with the design of such powers globally; the Australian Federal Treasurer, the Canadian Finance Minister and the United States’ President are responsible for exercising similar powers.

#### **4.2.2 Recommended option: replace the counterfactual with a ‘before and after’ test to determine whether an investment is beneficial**

136. We recommend a new ‘before and after’ counterfactual test involving a comparison of the applicant’s plans to the state of the land (and activities on it) at the time the application is lodged (that is, the current state). This is the test that the OIO used prior to the proposed acquisition of “Crafar Farms” by Milk NZ in 2012.<sup>23</sup>
137. The ‘before and after’ test would make it significantly easier for applicants and decision-makers to identify benefits, as this would remove the hypothetical element of the existing counterfactual test. This would make the test less complex, speculative and time-consuming and have a moderately positive impact on investment.
138. The changes would have a neutral to moderately negative impact on the government’s ability to manage risk. While it will make it easier to satisfy the benefits test in some cases, particularly for greenfields sites, the Government can manage significant risks through the new proposed national interest test and by adopting the proportionate approach discussed further below. This would require that benefits be proportionate to the sensitivity of the investment in all cases.
139. To address the issue of stranded assets and improve the chance of transactions involving high performing assets receiving consent:
  - a the broadly framed economic factor in the simplified benefits test would enable decision makers to consider a reduction in the risk of an asset being stranded as a benefit (e.g. through increased liquidity); and
  - b applying a proportionality approach to all transactions would lower the threshold for demonstrating benefits where an asset was already in overseas ownership.
140. If you wanted to take additional steps to reduce the chance of high performing assets being stranded, these mechanisms could be supplemented by the introduction of a ‘no detriments’ test. This is discussed in section 4.2.3.

#### ***Alternative option: comparison with what would happen if vendor continues to own the land***

141. An alternative option would be a comparison of an overseas person’s plans with what would happen if the vendor continued to own the land. This would place greater emphasis on risk management, but do less to resolve issues associated with the current counterfactual test.
142. The option would have a neutral or small negative impact on the ability to manage risk. As with the recommended option, there would no longer be a possible theoretical link to an alternative New Zealand purchaser. This would produce a lower threshold for satisfying the test in some cases, but is not a significant departure from the current test as a ‘continued ownership by the vendor’ threshold is often applied.<sup>24</sup> The option would continue to give some consideration to what might happen if the land was not acquired by the applicant (a hypothetical question), and therefore seeks to exclude from consideration benefits that would have arisen irrespective of the investment.
143. This option would have a relatively small positive impact on predictability, timeliness, and attractiveness to overseas investment. The main improvements arise from removing the concept of a “competent and adequately funded alternative New Zealand purchaser”,

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<sup>23</sup> Tiroa E & Te Hape B Trusts v Chief Executive of Land Information [2012] NZHC 147.

<sup>24</sup> The threshold was directly applied in just under 30% of recent cases, and may be used as a proxy for the alternative New Zealand purchaser counterfactual, which was used in about 66% of recent cases.

which can be more difficult to apply. The more significant problems associated with determining the likely future use of the land, however, would remain. The test would continue to require a degree of theoretical analysis, as in many cases a vendor has decided to sell, such that a counterfactual based on their continued ownership is hypothetical (and in the view of some submitters, illogical).

***Alternative or complementary option: Introduce a ‘no detriments’ test for asset sales between overseas persons***

144. A further option, which could complement either our preferred or alternative approach to the counterfactual, is a ‘no detriments’ test for sales between overseas persons, requiring only that the purchaser retain current benefits associated with the land and continue to comply with any ongoing conditions. This would seek to reduce the risk of large, well-managed assets being stranded because a potential purchaser cannot demonstrate incremental benefit.
145. A ‘no detriments’ test for sales between overseas persons could improve predictability and timeliness in relation to these transactions, but there are several design questions that would introduce further complexity (e.g., defining the degree of similarity required between the size and nature of the vendor and applicant’s investments, and potentially excluding certain sensitive categories of land, such as farmland).

***Option not progressed***

146. We also consulted on tweaking the current test to provide greater certainty about the applicable counterfactual (providing that where genuine market testing has shown that there is no domestic interest in the relevant land, the relevant counterfactual is the vendor’s continued ownership of the land). We do not recommend progressing this option as it would not reduce the test’s theoretical nature.

**4.2.3 Recommended option: replace the ‘substantial and identifiable’ threshold with a general proportionality requirement to ensure that benefits required to receive consent reflect the asset’s sensitivity**

147. We recommend replacing the “substantial and identifiable” benefit threshold for non-urban land greater than five hectares with a new statutory requirement that decision-makers take a proportionate approach to all applications subject to the benefits test.
148. The OIO already takes a proportionate approach to assessing whether the benefits of an application are sufficient to satisfy the benefits test. It takes into account the nature of the land (size, monetary value, sensitive features), and the interest being acquired (e.g. temporary or permanent, minority or majority shareholding). A legislative requirement would codify this approach.
149. The proposed changes would:
- a reduce the complexity of screening by removing the “substantial and identifiable” threshold that is overlaid across the benefits test, counterfactual test and proportionate approach;
  - b provide a legislative foundation for the OIO’s proportionate approach, confirming that applicants must demonstrate a level of benefit that is proportionate to the sensitivity of the asset, reflecting that it is a greater privilege for an overseas person to own or control more sensitive assets; and
  - c replace the current, relatively blunt legislative mechanism for achieving proportionality (under which a single land type – non-urban land – triggers a higher benefit requirement), with a requirement that decision-makers take into account the relevant

land's sensitive characteristics as well as features of the transaction (for example, the level of New Zealand involvement or the size of the interest being acquired).

#### **4.2.4 Overall assessment of benefits test reforms**

150. Our proposed package of reforms would significantly improve the government's ability to manage the potential risks of overseas investment, by providing for a more holistic assessment of proposed transactions and enabling the Minister to consider higher risk investments under the national interest test.
151. It also better manages the risk of stranded assets, by ensuring decision makers can take account of liquidity impacts as a part of the broadly framed economic benefits factor and proportionate approach.
152. Overall, the proposed package will have a moderately positive impact on predictability and transparency. While the national interest test will create more uncertainty for higher risk transactions, the simplified benefits test and the 'before and after' counterfactual will result in greater certainty and time and cost savings for the majority of applications. For these reasons, the proposed package will also have a moderately positive effect on New Zealand's attractiveness to overseas investment.
153. Codifying a proportionate approach to assessing benefit is likely to have a neutral or moderately positive impact on both risk management and predictability, as it is consistent with the OIO's current practice.

### 4.3 Should statutory timeframes be introduced in the Act?

Option	Impact summary		
<i>Recommended option:</i> tailored deadlines and an ability to extend, with an initial period for OIO to review an application and request further information before accepting an application.	Manage the risks of investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
	Neutral	Moderately positive	Moderately positive

154. There are no time limits for decisions on applications for consent. While the OIO has agreed several key performance indicators with Ministers for different types of consent applications, these are not binding. OIO data suggests that it takes around 100 working days on average for an application under the Act to be processed.<sup>25</sup>

#### ***Uncertainty about timeframes for decision-making is reducing New Zealand’s attractiveness to investment***

155. Most investors and professional advisors submitted that uncertain timeframes for decisions are the most serious issue with the Act. While there are several contributing factors (including current complexity in the consenting framework), there was overwhelming support for introducing statutory timeframes. Submitters highlighted that unpredictable timeframes for decision-making have resulted in transactions that would likely benefit New Zealanders not proceeding.

#### ***Recommended option: introduce tailored deadlines with an ability to extend, combined with the OIO having a specified period to review an application***

156. Introducing statutory timeframes would address the main concern expressed by submitters and bring New Zealand into line with other jurisdictions. The purpose of timeframes would be to set expectations about the depth of enquiry expected during the screening process, improving predictability for investors and increasing decision-makers’ accountability. We recommend that:

- a timeframes be tailored to each of the Act’s consent pathways;
- b decision makers be empowered to unilaterally extend timeframes by up to a prescribed period;
- c the OIO have an initial specified period (e.g. 15 working days) to review an application, and request any additional information, before accepting it.<sup>26</sup>

157. Timeframes would not start until after the application was accepted (that is, after any additional information is provided following the OIO’s initial review period).<sup>27</sup> Decision makers would still be entitled to seek additional information at a later stage, however doing so would not stop the clock on the relevant statutory timeframe.<sup>28</sup>

158. We recommend that specific timeframes are decided once Ministers have agreed on the overall reform package, as the choices made will determine what timeframes are reasonable. All parts of the application process, including time for Ministerial review, consultation with third parties, and any further information that is requested from

<sup>25</sup> This includes periods when the OIO has sought and is waiting to receive additional information from overseas persons. Overseas persons have advised that it can take up to one year (in total) to receive a decision.

<sup>26</sup> Changed fee structures that may be required to support this approach.

<sup>27</sup> Note the proposed initial review period is analogous to the QA period that the OIO currently apply before accepting an application.

<sup>28</sup> This is consistent with the Canadian regime.

applicants would need to be completed within the applicable timeframe. Timeframes should be set such that applications are processed more quickly than they are currently, while allowing sufficient time to fulfil natural justice requirements, where an application is being proposed to be declined. Applicants must be given an opportunity to respond to the proposal before the final decision is made.

***No automatic consent if timeframes breached***

159. The consultation paper tested whether applicants should automatically receive consent if decision-makers did not process an application within the prescribed time period. We do not recommend progressing this approach. Automatic consent would undermine the Act's purpose by making timing an overriding factor in decision making where no eligibility for investment has been demonstrated. It is also inconsistent with other New Zealand regulatory regimes that do not generally include automatic consent provisions if statutory deadlines are not met.

[36]

***Decision-makers should be able to extend the deadline once***

163. We recommend that decision-makers have the power to unilaterally extend a statutory deadline by up to a prescribed period (or an alternative agreed period). Providing for a single extension period increases predictability for investors, while recognising that, for particularly complex applications, some flexibility may be required.

164. We do not recommend enabling more than one extension period (whether unilaterally or by agreement with the applicant), because it would:

- a increase complexity and make any statutory timeframes less meaningful;
- b weaken the signal to the decision-maker as to the timeliness required by the Act; and
- c risk placing pressure on applicants to agree an extension to avoid the risk of an application being declined.

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[36]

### ***Reporting on timeframes***

165. We recommend decision-makers be required to publicly report on their compliance with statutory deadlines. This could include:
- a the reasons for and how often applications are extended;
  - b the reasons for and how often applicants are asked to provide further information; and
  - c the number of days it takes them to make each type of decision against prescribed deadlines.

### ***Assessment against reform objectives***

166. Statutory timeframes will encourage more predictable, transparent and timely outcomes, giving both decision-makers and applicants a better sense of how long the process should take. This will support overseas investment in productive assets.
167. We expect that introducing timeframes would, over time, lead to significant behavioural change by both applicants and the OIO, resulting in greater certainty for applicants, lower regulatory costs, and an increase in New Zealand's attractiveness to investment. This is because:
- a there would be additional incentives for applicants to submit high quality applications. The OIO would no longer engage in an iterative feedback process to allow submitters to provide additional information and may increase decline rates in the short-term as applicants' expectations adjust; and
  - b the decision-makers would be held publicly accountable to statutory deadlines, creating additional incentives to process applications more quickly.
168. There may be a marginal negative impact on the Government's ability to manage risk (if timeframes do not allow sufficient time for robust decision-making). The proposed approach would manage these risks by:
- a ensuring timeframes are appropriately calibrated to the different consent pathways (including sufficient time for Ministerial decision making);
  - b providing an ability to require further information before accepting an application (e.g. within the initial specified period to review an application);
  - c providing an ability to extend timeframes by a prescribed period; and
  - d the ability to decline applications where sufficient information has not been provided and/or the applicant has not met the statutory tests.
169. Residual risks could be addressed through additional resourcing and process improvements by decision-makers.

### ***Options not progressed***

170. We do not recommend imposing the same timeframe on all applications, as this would provide more time than necessary for some consent pathways, and insufficient time for others. Nor do we recommend timeframes commencing when an application is received or being paused if additional information is required. The ability to pause the timeline reduces predictability for investors. Commencing the timeline when an application is received would create an unfair burden on the decision-maker if delays were caused by waiting on additional information from applicants at the outset.

## Section 5: Proposals to strengthen the criteria for consent (how we screen)

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171. In line with the Terms of Reference, this section considers whether the benefits test should allow consideration of a prospective investment's effect on New Zealand's tax base, water extraction, or Māori cultural values. It also considers whether the requirements for farm land advertising are delivering on their objectives.
172. We recommend:
- a including non-compliance with tax law as a relevant offence or contravention in the proposed new investor test (this is considered under the status quo);
  - b clarifying and broadening the benefits test to allow recognition of protections for wāhi tūpuna or Māori reservations on sensitive land;
  - c broadening the benefits test to allow recognition of provision of access for the purposes of the stewardship of historic heritage and natural resources; and
  - d removing the requirement to advertise farm land.
173. These changes would improve the government's ability to manage risks, but generally would not significantly reduce the regime's transparency, predictability or regulatory burden.
174. We do not recommend expanding the benefits test to allow consideration of water extraction. The Resource Management Act (RMA) already exists as the principal tool for managing the environmental effects of water extraction, and the risks associated with water extraction are not specific to overseas investment.
175. Similarly, we do not recommend expanding the benefits test to consider an investment's effect on New Zealand's tax revenue. Tax legislation is the appropriate mechanism for managing tax risks.
176. Recognising widespread public concerns about these issues, we have developed alternative options that would expand the benefits test to allow consideration of water extraction, to consider an investment's effect on New Zealand's tax revenue. These options will add significantly more complexity and uncertainty to the regime, but not materially improve the Government's ability to manage risks.
177. [4]

## 5.1 Should a factor addressing water extraction be included in the benefits test?

Options	Impact summary		
	Manage the risks of investment	New Zealand's attractiveness to investment	Predictability, transparency and timely outcomes, decrease compliance costs
<i>Recommended option:</i> no changes to the benefits test in relation to water extraction	Neutral	Neutral	Neutral
<i>Alternative option:</i> include a factor in the recommended benefit tests that considers whether an investment that involves water bottling or bulk water extraction for human consumption will have a positive effect on water quality or sustainability.	Neutral	Moderately negative	Moderately negative
<i>Alternative option:</i> include a factor in the benefits test that considers whether an investment that involves water bottling, or in bulk water extraction for human consumption will have a positive or negative effect on water quality or sustainability.	Neutral	Strongly negative	Moderately negative

178. There are public concerns about overseas investments involving water extraction (particularly water bottling for export). These include the potential environmental effects and that overseas persons may profit from a high-value resource without paying a charge.
179. The RMA is the principal tool for managing the environmental effects of water extraction (including water bottling). It applies equally to New Zealanders and overseas persons and to all land (whether sensitive or not), and enables a consenting authority to consider impacts on a community's social, economic and cultural wellbeing (in addition to environmental effects).
180. The Act allows limited consideration of the environmental impacts of a proposed investment involving water extraction to the extent that water use relates to factors in the benefits test. Decision makers can currently consider whether there are mechanisms in place to protect or enhance significant indigenous vegetation or fauna, for example, but not the use of water.
181. We note the Government has a range of other work underway (including plans to introduce a royalty on bottled water, and *Essential Freshwater: Healthy Water, Fairly Allocated*) that could better address these concerns.

### **Consultation highlighted strong and divergent views on water**

182. There were strong and divergent views on what the Act's role should be in relation to managing risks to water supply and quality. Individual submissions strongly favoured increasing the Act's ability to screen water use by overseas persons. Many of these submissions focused on the exporting of water, rather than water bottling specifically. Concerns also often focused on the impact of the exporting of water on water quality and sustainability.

183. In contrast, the business community generally consider that the Act should not deal with water issues and support the status quo. Consistent with our view, they noted that the RMA already exists to regulate water use in New Zealand.

***Recommended option: make no changes to the benefits test in relation to water extraction***

184. The Overseas Investment Act cannot comprehensively address concerns about water extraction. Any change would only apply to overseas persons extracting water on sensitive land, or through a significant business asset. The Act is unable to screen transactions involving overseas persons bottling water on non-sensitive land<sup>[36]</sup> or not involving sensitive business assets.

185. The Act already makes reasonable provisions to address economic, environmental and cultural concerns that might result from water extraction on sensitive land. These considerations have limits (for example, at the moment environmental factors are mostly limited to ensuring there are adequate protections in place for native flora and fauna), but there is not strong justification for broadening these protections with respect to water, considering the role of the RMA.

186. The proposed inclusion of a broadly framed environmental factor in the benefits test will provide further opportunity for the Act to address concerns that might result from water extraction on sensitive land.

187. If you wish to make specific changes to the benefits test in relation to water extraction, we have identified two alternative options.

***Alternative option: include a positively-framed factor in the benefits test screening applications involving water extraction for bottling, or in bulk for human consumption***

188. This option would include a positively framed factor related to water extraction in the benefits test. You could adopt this option regardless of whether the benefits test enables consideration of negative factors. It would focus on managing the risks of overseas investment on the small number of applications that appear to be of the most concern – those involving water bottling. To address the main concern associated with this use of water, the criteria in the benefits test should focus specifically on water quality and sustainability.

189. Although the factor would only capture a small number of applications, and applicants would be able to cite benefits against clearly defined criteria (“water quality and sustainability”), targeting a specific issue already managed by the RMA would send a negative signal about New Zealand’s openness to investment. It would not provide Ministers with significantly greater discretion over affected applications, as applicants could still meet the benefits test by citing other factors.

190. For affected applications, there would be a minor negative impact on predictability, transparency and timely outcomes, and an increase in compliance costs (due to there being an additional factor in the benefits test to consider).

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<sup>30</sup> Land is screened under the Act if it is defined as ‘sensitive’.<sup>[1,36]</sup>

***Alternative option: include a factor able to be considered positively or negatively in the benefits test screening applications involving water extraction for bottling, or in bulk for human consumption***

191. This option only differs from the above in that it would include a factor related to water extraction in the benefits test, but decision-makers could consider both the positive *and* negative effects of a proposed investment. Choosing this option results in you adopting an alternative benefits test option that allows consideration of negative effects. Ministers would have greater discretion over affected applications, as although applicants could still meet other factors within the benefits test, Ministers could put greater weighting on the risks to water quality and sustainability.
192. For affected applications, there would be a negative impact on predictability, transparency and timely outcomes, and an increase in compliance costs. Unlike the previous alternative option, not providing sufficient benefit in relation to this factor could directly contribute to decision-makers declining an application. This would send an even more negative signal than the previous option about New Zealand's openness to investment.

***Options not recommended***

193. We do not recommend screening applications to extract water for any consumptive purpose, as opposed to focusing on extraction for bottling and in bulk for human consumption. This option was included in the consultation document. This definition of water extraction would result in screening a range of water uses, rather than focusing on those of the most concern to New Zealanders.
194. We do not recommend progressing the option of screening applications against the criteria of "wider economic, environmental, cultural and social concerns". The lack of a clear benchmark for these criteria would create uncertainty, creating a less predictable and transparent process, and it would not target the main concern of water quality and sustainability.

## 5.2 Should tax be considered as part of the consent process?

Options	Impact summary		
<i>Recommended option:</i> rely on the investor test to ensure that tax offences or contraventions resulting in a pecuniary penalty can be considered by decision makers (status quo)	Manage the risks of investment	New Zealand's attractiveness to investment	Predictability, transparency and timely outcomes, decrease compliance costs
	Neutral	Neutral	Neutral
<i>Additional option 1:</i> include a factor in the recommended benefit tests that considers whether an investment will have a positive effect on New Zealand's tax revenue	Neutral	Strongly negative	Moderately negative
<i>Additional option 2 (if negative impacts assessment is adopted):</i> include a factor in the benefit tests that considers whether an investment will have a positive effect on, or present a risk to, New Zealand's tax revenue	Moderately positive	Moderately negative	Moderately negative

195. There are public concerns about overseas persons acquiring sensitive New Zealand assets and paying a low level of income tax in New Zealand. This could be viewed as contrary to the Act's purpose, which recognises that it is a privilege for overseas persons to own or control such assets.
196. The Income Tax Act 2007 (Tax Act) and international agreements are the main tools for regulating income tax in New Zealand. This recognises that the imposition of income tax is an issue with domestic and international dimensions. The Tax Act reflects international best practice in this area by:
- a appropriately limiting double taxation that could reduce New Zealand's attractiveness to productive overseas investment; and
  - b maintaining New Zealand's tax base by limiting tax minimising activities.
197. Ministers are currently unable to consider an investment's potential impact on New Zealand's tax base through the benefits test. Compliance with tax law can be considered as part of the investor test.

### **Consultation highlighted mixed views on introducing additional tax considerations**

198. Submitters from the business community strongly opposed any change to the status quo and consider that the OIO is not well equipped to evaluate (especially foreign) tax compliance. Submitters consider New Zealand's existing tax laws already address ongoing tax compliance with respect to the investment, and that the investor test already appropriately considers an investor's past compliance record.
199. If an option was adopted, a small number of business submitters, including the Corporate Taxpayers Group<sup>31</sup>, favoured requiring larger investments to obtain a binding ruling from Inland Revenue.<sup>32</sup> This was an option included in the consultation document.

<sup>31</sup> The Corporate Taxpayers Group is a body of 45 large taxpayers. A number of other submitters, including BusinessNZ, also deferred to its submission on tax matters.

<sup>32</sup> Option 3 in the consultation document was to require overseas persons to obtain a binding ruling from Inland Revenue that the tax arrangements relating to the investments comply with New Zealand law.

200. Most individual submitters considered that tax should be an important factor in determining consent. These submitters argue that overseas investors must pay for the services they receive and that previous tax compliance is a reliable indicator of future behaviour. Most submitters did not nominate a preferred option, but appeared to prefer explicitly incorporating tax into the investor test.

***Recommended option: rely on the investor test to ensure that decision makers can consider tax offences***

201. Currently, the Act requires any breach, or allegations of a breach, of tax law by individuals with control to be considered in the investor test.<sup>33</sup> We are proposing changes to the investor test that would narrow the matters that may be taken into account to certain types of offences and contraventions. Consistent with this proposal, we recommend that tax offences punishable by imprisonment and tax contraventions resulting in a pecuniary penalty be included either explicitly or generally. Serious, deliberate breaches of tax law are relevant to determinations of character, and can be indicative of future action in New Zealand.

202. Following discussions with Inland Revenue, we understand that significant penalties (eg. shortfall penalties for tax evasion) can be imposed by tax authorities rather than a court. These breaches are not captured in our recommended options for tax or the investor test. If you adopt our recommended approach to the investor test, we will provide further advice on whether these should also be captured.

203. Removing decision-makers' ability to consider serious tax offences as part of the investor test would reduce the Governments' ability to manage the tax risks associated with foreign investment.

204. We have also recommended that the investor test apply to bodies corporate. This means that decision makers will be able to consider tax offences or contraventions committed by bodies corporate. Under the status quo, a body corporate's activities can only be considered if those activities can be imputed to individuals with control.

205. We have considered whether, in addition to the proposed approach to the investor test, the benefits test should include a factor related to tax. We have considered two alternative approaches, discussed further below.

***Additional option 1: include a factor related to an investment's positive effect on tax revenue in the recommended benefits test***

206. Post-consultation, we developed an additional option with Inland Revenue. This option would allow Ministers to consider whether an investment would, or would likely, have a positive effect on New Zealand's tax revenue under the benefits test. Inland Revenue would conduct a high level review of transactions to assess likely outcomes against this factor. This would complement the consideration of tax compliance under the investor test.

207. This option would moderately improve the Government's ability to manage the tax risks associated with foreign investment by giving Inland Revenue some visibility over overseas persons' tax arrangements. This would help Inland Revenue when monitoring those overseas persons for compliance with New Zealand tax law.

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<sup>33</sup> The investor test allows the decision maker to take any offences or contraventions of the law as part of the good character criterion.

208. However, because overseas persons will generally pay less New Zealand income tax than New Zealanders due to tax obligations in other countries<sup>34</sup>, an investment by an overseas person would not generally be expected to increase overall levels of New Zealand income tax (even in the absence of any tax avoidance or minimisation behaviour). This would mean an overseas person would generally not meet this element of the benefits test unless:
- a the sale was between overseas persons (in which case the other overseas person may be paying a similar amount of New Zealand income tax); or
  - b the purchaser was scaling up the business. However, while this would create a positive benefit, we consider that benefit is most appropriately assessed by measuring the growth in the business via the economic benefit factor rather than tax revenue.
209. This option is inherently limited because it would only allow tax to be considered in respect of transactions to acquire sensitive land, not transactions involving significant business assets only.<sup>35</sup>
210. Further, while offering limited benefits, this option would add additional compliance costs for investors and reduce timeliness, particularly if a prospective investor had to change its structure in order to meet the factor. These additional compliance costs would reduce the Act's ability to support productive investment.
211. Consequently, we do not recommend this option. Tax law (or more specifically, international tax law) is the Government's best tool to manage tax risks associated with foreign investment. It responds to the perceived issues in a uniform way across all entities that do business in New Zealand. In contrast, the Act cannot respond to the problem comprehensively due to its application being limited to a narrow section of investment.

***Additional option 2: include a factor related to an investment's positive effect on, or risk to, tax revenue in the benefits test***

212. This option would be similar to 'additional option 1', however the Government would be able to consider the positive and negative effects of an investment on New Zealand's tax revenue (rather than just the positive effects). Unlike the previous option, choosing this option results in you adopting an alternative benefits test option that allows consideration of negative effects.
213. The focus of the negative impacts assessment would be whether a transaction presents a risk to New Zealand's tax revenue or the integrity of the tax system.<sup>36</sup> If there was a risk, and that risk was not offset by other benefits of the investment, an overseas person would be given a chance to alter the structure of the transaction (e.g. adjust the debt to equity ratio of funding) to improve its chances of obtaining consent (this could also occur under additional option 1 but it would be less likely).
214. We do not recommend this option. Like additional option 1, this option would have limited application and would significantly increase compliance costs. Although it would improve the Act's ability to mitigate risks to tax revenue, expanding the scope to negative effects is also likely to reduce timeliness and increase administrative costs (when compared to the status quo and additional option 1). This would send a negative signal about New Zealand's openness to investment.

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<sup>34</sup> Overseas persons may have income tax obligations in other countries. Double taxation agreements limit a country's ability to impose income tax where this would result in double tax liability.

<sup>35</sup> 29% of applications feature significant business assets and less than half of those are subject to the benefits test (because these transactions do not involve sensitive land).

<sup>36</sup> This is broadly consistent with the treatment of tax by the Australian Tax Office when advising Australia's Foreign Investment Review Board.

***We have not progressed the option of requiring overseas persons to obtain a binding ruling***

215. Requiring overseas persons to obtain a binding ruling is not a viable option. It would increase compliance costs and significantly reduce timeliness<sup>37</sup> without improving the Government's ability to manage tax risks. This is because a binding ruling would assess the legality of the proposed tax treatment of an arrangement, but not the impact of a transaction on New Zealand's tax revenue (which appears to be the main public concern).

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<sup>37</sup> Inland Revenue take up to 10 weeks to prepare a draft binding ruling on less complex issues. A draft ruling on more complex issues can take up to six months. Rulings cost between \$5,000 and \$45,000. The average fee is \$15,000.

### 5.3 Should a factor addressing Māori cultural values be included in the benefits test?

Options	Impact summary		
<i>Recommended option:</i> clarify and broaden the benefits test to allow recognition of protections for wāhi tūpuna or Māori reservations on sensitive land	Manage the risks of investment	New Zealand's attractiveness to investment	Predictability, transparency and timely outcomes, decrease compliance costs
	Neutral	Neutral	Neutral
<i>Recommended option:</i> broaden benefits test to allow recognition of provision of access for the purposes of the stewardship of historic heritage and natural resources	Moderately positive	Neutral	Moderately negative

216. Consultation, submissions on the past reforms of the Act, and protests about particular applications indicate a degree of public concern that the Act does not sufficiently recognise Māori cultural values. Concerns appear to relate particularly to awareness of, and protection for, sensitive sites, and Māori relationships with those sites, particularly where land has been lost through confiscation or an acknowledged breach of the Treaty of Waitangi.
217. These concerns may relate to land ownership or to land use. Where these concerns arise from historical associations with the land in question, ownership will be the primary issue. Where concerns arise from cultural values associated with the natural world, land use and activities will be the primary issue. The RMA is the principal tool for managing land use. It specifies that the relationship of Māori and their culture and traditions with their ancestral lands, water, sites, wāhi tapu and other taonga (*treasures*) is a matter of national importance to be recognised and provided for.
218. The Overseas Investment Act expressly allows decision-makers to consider an applicant's proposed protections for the cultural qualities of natural and physical resources and sites of significance to Māori, such as wāhi tapu as part of the historic heritage factor in the benefits test. The OIO recommends that overseas persons consult iwi on applications that appear to involve sites of particular significance to Māori. This assists with identification of historic heritage and helps confirm that any recommended protection mechanisms are appropriate.

#### **Consultation highlighted mixed views on greater recognition of Māori cultural values**

219. Submitters had mixed views about whether the Act should provide greater recognition of Māori cultural values. Most acknowledged the special significance of land and resources in te ao Māori, and some also noted the Treaty principles of partnership and active protection. Iwi representatives, individual submitters, and hui attendees supported increasing recognition of Māori cultural values. Many of the professional advisers did not consider there to be a need for greater consideration of cultural values in investment screening.
220. The preferred option from within the consultation document (particularly among professional advisers and investors) was to slightly clarify and broaden the benefits test to expressly recognise wāhi tūpuna and Māori reservations as historic heritage.

221. A number of submitters, particularly iwi representatives, also suggested alternative approaches that could enable the better identification of sensitive sites and appropriate conditions to be applied, and enhance overseas persons' cultural awareness. The most common suggestion was to require the OIO or applicants to consult mana whenua. This was seen as particularly important for protecting sensitive sites that may not appear in government records.

***Recommended option: amend the 'benefit to New Zealand' test and make some operational improvements to give greater recognition to Māori cultural values***

222. We propose legislative changes that could enable Māori cultural values to be further reflected in the benefits test by enabling decision-makers to take account of overseas persons' intentions to:

- a protect or enhance wāhi tūpuna that are listed under the Heritage New Zealand Pouhere Taonga Act 2014,<sup>38</sup> and/or Māori reservations.<sup>39</sup> Including reference to these sites will encourage an applicant to check for their presence, and recognise important sites in a manner more culturally relevant in te ao Māori; and
- b provide, protect or enhance access within or over land for the purposes of undertaking activity like the stewardship of historic heritage and natural resources. This is a revision of the option consulted on, and responds to feedback that the previous option was too narrow and had an unclear purpose. We would seek to align changes with any similar reforms to the Walking Access Act 2008, which is currently being reviewed.

223. Both options would better manage potential risks of overseas investment by supporting:

- a informed decision-making, as there would be greater awareness amongst applicants and the OIO about the existence of sensitive sites and appropriate mechanisms to protect and manage access; and
- b greater awareness of tikanga Māori and attention to relationships with tangata whenua among overseas persons, which could then inform their ongoing management of the land.

224. These proposals are not expected to materially affect New Zealand's attractiveness to investment. However, applications where access was negotiated would require the OIO to spend additional time preparing, assessing and monitoring the investment.

225. A legislative requirement for applicants or the OIO to consult Māori is out of scope of the review. However, there are operational changes that the OIO and investors could make to support greater awareness of Māori cultural values and sensitive sites. The OIO is currently exploring ways for more productive engagement with external stakeholders. This includes reviewing and updating resources and procedures to ensure that all relevant considerations, including historic heritage, are appropriately and efficiently identified and assessed. There are opportunities to improve guidance to assist applicants to identify sites sensitive to Māori and to contact iwi. [33]

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<sup>38</sup> A place important to Māori for its ancestral significance and associated cultural and traditional values.

<sup>39</sup> As established in Te Ture Whenua Māori Act, section 338, which broadly include sites of ancestral, historical, spiritual or emotional significance to Māori.

### ***Options not assessed***

226. We have not recommended options allowing or requiring decision-makers to consider Māori cultural values generally as part of the benefits test. Te Arawhiti advise that not requiring decision-makers to do this may pose a risk to Māori wellbeing.
227. We consider that on balance, the recommended options best satisfy the objectives of the reform. Unlike the recommended options, a broadly framed factor would not provide clear direction about the nature of values that could be protected through screening. This would therefore create significant uncertainty, potentially undermining the option's effectiveness at addressing areas of particular concern with the benefits test and therefore effectiveness at managing the risk of overseas investment. Additionally, it could produce a less predictable and transparent process, and therefore reduce attractiveness to investment.

## 5.4 Should the requirement to advertise farm land be removed or improved?

Options	Impact summary		
	Manage the risks of investment	New Zealand's attractiveness to investment	Predictability, transparency and timely outcomes, decrease compliance costs
<i>Recommended option:</i> remove the requirement to advertise farm land	Neutral	Moderately positive	Strongly positive
<i>Alternative option:</i> clarify farm land advertising rules, require advertising before transaction, and improve exemptions process.	Moderately positive	Neutral	Strongly positive

228. Farm land must be advertised for sale on the open market before consent can be given to an overseas person to obtain an interest in it (unless an exemption has been granted). This requirement intends to ensure that New Zealanders have the opportunity to acquire, enjoy and use farm land.

229. Current requirements are overly complex and are not meeting the Act's objectives:

- a the advertising is often not genuine as the requirement can be met after a conditional sale and purchase agreement (or other form of agreement) has been entered into;
- b the minimum advertising standards are ineffective (for example, a vendor can meet the requirements by placing a placard on the relevant land); and
- c the process lacks flexibility. Before consent can be granted, the advertising requirement must be met, or the transaction must meet set criteria in order to be exempted from the requirements entirely. There is no middle ground (for example, allowing an alternative form of advertising, better suited to the circumstances).

### **Submitters expressed mixed views**

230. Individuals and interest groups supported retaining the requirements on the basis that New Zealanders should have the opportunity to acquire farm land. Law firms and businesses submitted that the provisions are unnecessary as a vendor has an interest in testing the market, where appropriate, to maximise their sale price.

231. The consultation paper sought feedback on removing the requirement to advertise farmland, or clarifying the requirements.

232. When assessed against criteria for reform, these options are finely balanced. Given that in the majority of cases we would expect advertising to occur anyway if a vendor is genuinely prepared to consider competing offers (to maximise the sale price), we recommend removing the requirement. We recognise, however, that there are legitimate policy objectives for retaining and clarifying the requirement.

### **Recommended option: Remove farm land advertising requirements**

233. Some submitters suggested that the requirements are unnecessary, as vendors are likely to advertise their farmland's sale, in order to maximise their sale price. If vendors do not wish to test the market, the reasons for not doing so will likely mean they have little interest in competing offers resulting from advertising.

234. Removing the requirement to advertise farm land would reduce compliance costs and complexity, increasing New Zealand's attractiveness to investment. However, this option would reduce the Government's ability to ensure that New Zealanders have an opportunity to purchase the land before overseas persons acquire it.

**Alternative option: Clarify farm land advertising requirements**

235. If the farm land advertising provisions are to be maintained, we recommend the following changes and clarifications to ensure farm land advertising is genuine and accessible to the public, while also allowing flexibility to manage complex cases:

- a requiring advertising before an owner and overseas person enter into a transaction (noting that the overseas person could still make an offer)<sup>40</sup>;
- b requiring at least two forms of prescribed advertising, removing 'notice' and 'placard' as appropriate forms of advertising, and increasing the minimum advertising period to allow time for due diligence on high value investments<sup>41</sup>;
- c clarify that the OIO can approve alternate advertising plans in situations where the prescribed requirements are unsuitable;
- d clarify that only the interest in land being acquired has to be offered for acquisition on the open market (e.g. if the vendor is offering a 50-year lease, then a 50-year lease must be advertised); and
- e improving the process for exemptions from the advertising requirements including:
  - i clarifying that an exemption application may be submitted and decided before an application for consent is lodged and that the OIO can charge a fee for doing so. This would enable certainty about the application of the farm land advertising requirement before an overseas persons applies for consent;
  - ii clarifying that the OIO can impose conditions on exemptions to ensure that they are not used to circumvent advertising requirements; and
  - iii providing guidance that clarifies where discretionary exemptions should be granted by specifying the intent of the farm land advertising requirement and including some criteria for exemptions.

236. Strengthening the current requirements would enhance the government's ability to manage the risk of overseas investment by better allowing New Zealanders the chance to purchase farm land, recognising the ownership value New Zealanders place on farm land. It would not reduce New Zealand's attractiveness to investment because increased stringency of the rules (by requiring advertising before a transaction) is balanced by a clearer process and more flexibility to make exemptions.

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<sup>40</sup> Framing it in this way would mean advertising requirements are triggered by a broad range of agreements (including 'arriving at an understanding' between the vendor and overseas person), not just written agreements.

<sup>41</sup> More targeted consultation with industry would be needed to identify a reasonable timeframe. Note the current minimum advertising period is 20 working days.

[4]

## Section 6: Proposals to reduce the screening of lower risk transactions (what and who we screen)

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243. This section proposes reforms to reduce screening requirements for low risk investors and investments. In particular, we propose changes to the definition of sensitive adjoining land and treatment of leases, as well as reforms to who we screen and when.
244. We recommend:
- a significantly narrowing the definition of sensitive adjoining land (retaining narrow categories of land that adjoin foreshore, lakebeds and some land significant to Māori);
  - b only screening leases with terms of 15 years or more for all assets except residential land (where the current threshold of three years or more would be retained);
  - c narrowing the definition of “overseas person” for New Zealand incorporated and listed bodies corporate that are majority owned and controlled by New Zealanders;
  - d introducing new exemptions for New Zealand incorporated companies and managed investment schemes that are majority owned and controlled by New Zealanders;
  - e amending the existing exemption for retirement schemes that are controlled by New Zealanders, so that they are carved out of the definition of “overseas person”; and
  - f removing screening requirements for acquisitions that do not materially change overseas persons’ level of control over sensitive assets.
245. These proposals would narrow the Act’s scope and significantly reduce transaction costs for low risk investments and investors that are fundamentally New Zealand entities. These types of investments and investors do not pose a material risk to New Zealand and are not the Act’s intended targets. Accordingly, the recommended reform package has no material impact on New Zealand’s ability to manage the risks of overseas investment.
246. We also present alternative options. These options reduce the screening of lower risk transactions relative to the status quo, but to a lesser extent than the recommended package. They generally place greater weight on managing the risk of overseas investment rather than on encouraging it. Our alternative proposals include:
- a minor changes to the definition of sensitive adjoining land; and
  - b only screening leases with terms of 10 years or more (but retaining the three years or more threshold for residential land).
247. We have not proposed an alternative package in relation to who we screen and when. The preferred options are interdependent; should you wish to consider alternative options we will need to provide further advice.
248. [1, 36]

## 6.1 Should the scope of sensitive adjoining land be reduced?

Options	Impact summary		
<i>Recommended option:</i> remove Table 2 land from the Act, with the exception of land adjoining the foreshore, lakebeds and some land significant to Māori	Manage the risks of investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
	Neutral	Strongly positive	Strongly positive
<i>Alternative option:</i> retain most categories of Table 2 land, but remove section 37	Neutral	Moderately positive	Moderately positive

249. The Act requires transactions to be screened if they involve land that adjoins land with sensitive characteristics, such as the foreshore, a lakebed, some types of conservation land, historic places, and wāhi tapu (sacred places). We call this land with sensitive characteristics ‘Table 2 land’, referring to land listed in Table 2 in Schedule 1 of the Act.

250. Table 2 land includes land listed as a reserve, a public park or other sensitive area by the OIO under section 37 of the Act. The section 37 list currently includes all land over 0.4 hectares that a regional plan, district plan or proposed district plan designates as a reserve, as a public park, for recreation purposes or as an open space. It also includes national parks.

251. Some stakeholders have raised concerns that Table 2 land is broader than necessary to manage the risk of overseas investment, and creates unnecessary compliance costs. This adjoining Table 2 land is screened to ensure transactions are beneficial to the conservation of, or public access to, Table 2 land. Table 2 includes land with low or no environmental, cultural or access sensitivities. There is no clear rationale for screening investments adjoining this type of land.

252. The way land is treated under the Act depends on how individual local authorities designate it in their district plans. This means that land of similar sensitivity across New Zealand may not be treated consistently under the Act. It also increases the time and complexity associated with identifying whether land is sensitive.<sup>42</sup>

### Examples of sensitive adjoining land requiring investors to gain consent provided by submitters during consultation include:

- A supermarket adjoining a sports field. The business had operated a supermarket under a leasehold arrangement on the site since the 1960s, and was purchasing the freehold title.
- A supermarket adjoining a grass berm, classified as a reserve.
- A trade supplies store adjoining netball courts and zoned open space, easily accessible by a major road (and where access through the trade supplies store would create a significant health and safety risk).

<sup>42</sup> In some cases, a ‘sensitive land certificate’ may need to be obtained, at the overseas person’s expense, to determine whether the land is sensitive or not.

### **Consultation highlighted support for narrowing the scope of sensitive adjoining land**

253. Overall, submitters support narrowing the scope of sensitive adjoining land requiring consent. They agree the current regime is too broad and that there are particular issues with the section 37 list.

254. We consulted on two options to narrow the scope of Table 2 land. Most submitters (particularly industry groups, professional advisors and investors) supported removing Table 2 from the Act, except for the foreshore, lakebeds and some land significant to Māori. A smaller number supported only removing section 37 (in full or in part). Few submitters supported the status quo, or broadening the scope of sensitive adjoining land.

### **Recommended option: remove Table 2 land from the Act, with the exception of land adjoining the foreshore, lakebeds, some land significant to Māori**

255. This option would have no impact on the Government's ability to manage the risks of overseas investment. It would remove categories of land with no obvious sensitivities, while retaining the ability to screen land adjoining truly sensitive land (e.g. foreshore and lakebeds). The RMA, which regulates land use including impacts on adjoining land, adequately manages any residual risk.

256. Our recommended approach would limit the Government's ability to negotiate conditions on some investments, such as walking access, or the control of wildling conifers. However, environmental, cultural and access benefits are rarely applied, and are present at a much lower rate than in transactions for Table 2 land that include land sensitive in its own right.<sup>43</sup>

257. Removing Table 2 would both support productive investment in New Zealand, and deliver more predictable, transparent and timely outcomes, as it would reduce the number of sensitive land applications by approximately 10 to 14%.<sup>44</sup> It would address concerns that Table 2 land is negatively affecting New Zealand's ability to attract investment.

258. We recommend continued screening of land adjoining foreshore, lakebeds, some land significant to Māori. Screening land adjoining the foreshore or lakebeds is consistent with provisions in the RMA for the maintenance and enhancement of public access to coastal marine areas and lakes. Continuing screening adjoining land significant to Māori in Table 2 recognises the Crown's Treaty obligations.

#### **Land significant to Māori would include**

- A Māori reservation that adjoins the sea or a lake and to which section 340 of the Te Ture Whenua Maori Act 1993 applies.
- Land that is set apart as a Māori reservation and that is wahi tapu under section 338 of Te Ture Whenua Māori Act 1993.
- wāhi tapu or a wāhi tapu area under the Heritage List/Act.
- Reserves that are subject to the Reserves Act 1988 and are managed wholly or jointly by the governance entity of a collective group of Maori such as an iwi or hapu.
- Public conservation land that has been used as cultural redress in Treaty settlements and has retained conservation protection.

<sup>43</sup> Most of the benefits applied in applications where Table 2 land is the only sensitivity have no relevance to a transaction's particular risks to Table 2 land – such as “previous investments” (cited in 56% of all applications where Table 2 land is the only sensitivity).

<sup>44</sup> Based on previous application data.

259. [1, 36]

260. Previous application data shows most applications to acquire land adjoining Table 2 land also include land sensitive in its own right. The Act will continue to screen these types of transactions. In these cases, applicants will still be able to cite benefits (eg. environmental, cultural and access) relevant to the Table 2 land. The OIO will continue to be able to consult with affected parties like the Department of Conservation and Walking Access Commission on appropriate conditions.

***Alternative option: retain most categories of Table 2 land, but remove section 37***

261. This option would retain most Table 2 land, but remove section 37. It would continue screening the following categories of land captured by section 37:

- a national parks;
- b scientific, scenic, historic or nature reserves under the Reserves Act 1977 managed by local authorities and others (in addition to those administered by the Department of Conservation);
- c wildlife management reserves, refuges and sanctuaries under the Wildlife Act 1953;
- d reserves that are subject to the Reserves Act 1988 and are managed wholly or jointly by the governance entity of a collective group of Māori such as an iwi or hapu; and
- e public conservation land that has been used as cultural redress in Treaty settlements and has retained conservation protection.

262. As with the recommended option, there would be no impact on the Government's ability to manage the risks of overseas investment. The Government would retain greater ability to negotiate conditions on some investments that provide additional benefits to New Zealand, but it would do less to support productive investment in New Zealand, and deliver more predictable, transparent and timely outcomes.

263. This option would exclude most recreation reserves from screening, as well as some government purpose and local purpose reserves. These are generally the reserves of the lowest environmental concern (reflected by their status in the Reserves Act 1977). They can also usually be accessed via public roads or tracks.

[1, 36]

265. Some submitters suggested an alternative consent pathway for transactions involving only Table 2 land (for example, only requiring the applicant to commit to any benefits provided by the existing owner, such as access arrangements). If Ministers prefer this alternative option that retains Table 2, we will provide further advice on options for an alternative consent pathway to reduce the compliance costs associated with Table 2 land.

***Options not progressed***

266. Some submitters suggested broadening the scope of Table 2 land, and the Department of Conservation suggested including Significant Natural Areas (SNAs) on public land in screening. [1, 36]

## 6.2 How should the Act treat leases and other less-than freehold interests in land?

Options	Impact summary		
<p><i>Recommended option:</i> screen leases over sensitive assets with terms of 15 years or more</p>	Manage the risks of investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
Continue to screen all leases of residential land of three years or greater	Neutral/moderately negative	Moderately/strongly positive	Moderately positive
<p><i>Alternative option:</i> screen leases over sensitive assets with terms over than 10 years or more</p> <p>Continue to screen all leases of residential land of three years or greater</p>	Neutral/moderately negative	Moderately positive	Moderately positive
<p><i>Complementary option:</i> screen leases over sensitive assets that cumulatively result in the leasehold threshold being exceeded</p>	Moderately positive	Moderately negative	Neutral
<p><i>Recommended option:</i> Clarify that periodic leases are not an interest in land</p>	Neutral	Neutral	Moderately positive

267. Currently, leases and other less-than freehold interests in sensitive land with terms of three years or greater are captured by the screening regime. Less-than freehold interests include legal or equitable interests, such as *profits à prendre*.<sup>45</sup>

268. In general, leases are viewed as less sensitive than freehold interests because they are of limited duration and the benefit and use of land ultimately returns to the current owner. This often results in an asymmetry between the cost of the screening process and the more limited level of control that lessees generally have over land.

269. However, in some cases the nature of the lease can confer rights that are similar in nature to freehold transactions, particularly where the lease is long term. In these cases screening is appropriate. There may also be risk stemming from the nature of the assets being leased (for example, environmentally sensitive sites), and general avoidance risk, if investors choose to take up shorter leases to avoid screening. The proposals aim to set the right threshold to balance compliance costs against the risks associated with leases.

270. There is an additional technical issue related to periodic leases.<sup>46</sup> These interests have never been screened under the Act, however changes in 2018 that clarified their treatment in respect of residential land have created uncertainty about whether periodic leases over other types of sensitive land require consent.

<sup>45</sup> Less-than freehold interests can include options, leases, profits à prendre and mortgages. For the balance of this section, “leases” refers to both leases and other less-than-freehold interests in land.

<sup>46</sup> Periodic leases have no set end date and continue until either party gives written notice to end the lease.

**Consultation highlighted support for increasing the time threshold for screening leases and other less-than freehold interests in land**

271. The majority of submitters (largely law firms, individual businesses and industry groups) supported extending the threshold for excluding leases beyond the current three years.
272. Stakeholders noted that it can be difficult to demonstrate benefit over shorter periods, and where they do not have full control of the asset. They also indicated that the complexity and delay associated with consents for leasing could make land owners reluctant to lease land to overseas persons and create incentives for overseas persons to purchase land, rather than leasing it (because compliance costs are similar).
273. We consulted on two reform options:
- a only screening leases of 10 years or more; and
  - b only screening leases of 10 years or more over non-urban land greater than five hectares, and leases for all other types of land with terms of 35 years or greater.
274. Most submitters considered that 10 years was still too short a timeframe for most commercial leases, suggesting terms ranging from 12 to 35 years. Most submitters did not see a rationale for treating different types of land differently (e.g. having different timeframes for non-urban land greater than five hectares) and preferred a uniform treatment.
275. [1, 36]

**Recommended option: Only screen medium term leases with terms of 15 years or more, except for leases of residential land, which would continue to be screened if they are of three years or more**

276. This option would have a marginally negative impact on the Government's ability to manage the risks of overseas investment. This is because it would remove a number of transactions that are currently screened from the regime<sup>47</sup> and limit the Government's ability to negotiate conditions on some investments that provide benefits to New Zealand (e.g. public access). We understand a 15 year term would mostly exclude commercial transactions (i.e. leasing of industrial land, retail or offices).
277. A 15 year term may capture some horticultural/agricultural/viticulture leases, but these leases are generally on longer terms. Some leases of this type may be able to be acquired by an overseas person without consent if, for example, they were only obtaining the remaining term on an existing longer term lease. The risk associated with this is low given that the use of the land will remain largely the same and extending the lease further would require consent.
278. There may be some risks associated with the proposal to increase the threshold for leases. For example, the uniform approach (other than residential land – discussed below), would mean that a less-than 15 year lease in any type of sensitive land, would be treated the same regardless of (for example) the size or environmental sensitivity of the

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<sup>47</sup> This option would have excluded approximately 10 of the 79 of applications (13%) involving leases assessed over the last five years.

property. Given the different levels of ownership value that New Zealanders place on different pieces of land, some may not view this as appropriate.

279. The proposal would also increase the risk of overseas persons entering into multiple consecutive leases below the threshold and obtaining an interest in totality that exceed the threshold without obtaining consent. The scale of this risk, however, is judged to be low. This is because:
- a investors will face commercial incentives to obtain certainty of tenure that in many cases will outweigh the cost of obtaining consent; and
  - b investments structured with the intent of avoiding screening under the Act would likely breach the Act's anti-avoidance requirements (noting that detection and enforcement may be difficult).
280. Despite these risks, on balance this option would both support productive investment in New Zealand, and deliver more predictable, transparent and timely outcomes, as it would significantly reduce compliance costs for a small number of transactions.
281. Last year's amendments to the Act brought residential land and *profits à prendre* (including forestry rights) into the screening regime. The threshold for screening these interests was set at three years, in line with the current timeframe for leases. We propose leaving the threshold for leases of residential land at three years to align with the Government's policy intent for the phase 1 reforms. It is also arguable that shorter term leases of residential land are more akin to ownership than they are for other types of sensitive land.
282. The rationale for removing the exemption that *profits à prendre* previously had under the regime was to ensure regulatory coherence as they are an interest in land that was not being screened. To ensure continued regulatory coherence, we consider that the term for screening *profits à prendre* should align with that proposed for leases (that is, the threshold for screening all less-than freehold interests should be the same).
283. [1, 36]

***Alternative option: a shorter-term for screening leases (screen leases of 10 years or more)***

284. An alternative approach is to screen leases with terms of 10 years or more. The threshold for screening residential land would remain three years.
285. The effect would be similar to raising the threshold to 15 years or more, however fewer transactions would be excluded. The option would place greater weight on managing the risks of overseas investment.

***Complementary option: Screen leases that cumulatively breach the adopted threshold***

286. Either the recommended or alternative option, if adopted, could be strengthened by also requiring investors to obtain consent when they enter into a single lease or consecutive leases that breach the threshold. For example, if an investor entered into a 10 year lease at the conclusion of a previous 10 year lease (where there was a 15 year threshold), the second lease would be subject to screening. This mitigates against the risk of investors entering consecutive medium term leases to avoid the need to obtain consent and would

remove pressure from the OIO where it believed that transactions had been structured to avoid the Act and enforcement action needed to be taken.

287. While this would marginally increase the government's ability to manage risks associated with foreign investment, it would increase the Act's complexity and may result in additional burden for investors. [1, 36]

***Recommended option: clarify that periodic leases are not an interest in land***

291. In addition to extending the threshold for screening leases, we recommend clarifying that periodic leases are not an interest in land that requires consent under the Act. This would be consistent with current practice and the treatment of residential land and therefore not reduce the Government's ability to manage risks. It would reduce uncertainty associated with the current legislative drafting, marginally improving the Act's ability to support productive overseas investment.

### 6.3 Who we screen and when – changes to the definition of “overseas person”, treatment of portfolio investors, and transactions that do not change who controls sensitive New Zealand assets

Options	Impact summary		
Narrow the definition of “overseas person” to exclude New Zealand incorporated and listed bodies corporate that are majority owned and controlled by New Zealanders	Manage the risks of investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
	Moderately negative	Moderately positive	Strongly positive
New exemption for New Zealand incorporated entities that are majority owned and controlled by New Zealanders and of good character	Neutral	Moderately positive	Moderately positive
New exemption for managed investment schemes that are majority owned and controlled by New Zealanders and of good character	Neutral	Moderately positive	Moderately positive
Amended exemption for retirement schemes, exempting them from the definition of overseas person rather than from consent requirements	Neutral	Moderately positive	Neutral
<i>Recommended option:</i> Only require consent if overseas persons increase their holding in a sensitive asset above the control limit (that is, 25, 50, 75 or 100%). Remove existing exemption for small incremental investments	Neutral	Strongly positive	Strongly positive
<i>Alternative option:</i> As per the recommended option, but retain regulation 38(2)(c)(i), so that an overseas person may increase an investment by 5% of the interest that they have consent to hold regardless of control limits [1]	Neutral	Moderately positive	Strongly positive
Only require overseas persons to get consent to invest in New Zealand incorporated and listed bodies corporate if the investment results in the target entity breaching the control limb of the definition of overseas person	Neutral	Moderately positive	Moderately positive

292. Overseas persons are generally required to obtain consent before they can acquire a 25% interest, or increase their interest, in sensitive assets (that is, sensitive land, significant business assets, and fishing quota). While this is generally appropriate, the rules are broadly cast and overreach in a number of ways, unnecessarily increasing the Act’s regulatory burden. In particular, the rules:

- a treat a range of fundamentally New Zealand entities as overseas persons;<sup>48</sup> and
- b require overseas persons to obtain consent for often small transactions where they obtain no control over the sensitive asset (the ‘tipping point’ problem), or their degree of control does not change (the ‘incremental investment’ problem).

<sup>48</sup> Under the Act, an entity is deemed to be an overseas person if it is 25% or more owned or controlled by overseas persons. This is the case irrespective of whether overseas persons could realistically exert control over sensitive assets – for example, where interests in the entity are widely held this is unlikely to be the case.

293. Separately, there are concerns that the Act is overly burdensome for portfolio investors making passive investments<sup>49</sup>. This type of investment is an important source of capital for New Zealand, can offer unique expertise to domestic partners, and is considered low risk.

294. We consulted on a range of options to resolve these problems.

***Consultation highlighted support for narrowing the definition of “overseas person”, including exemptions for portfolio investors, and carving out smaller transactions***

295. Most submissions on these topics came from businesses and their advisors. There was general agreement that the Act is overreaching in relation to who it screens and when.

296. There was widespread support for narrowing the definition of overseas person for New Zealand incorporated and listed bodies corporate. Of the options presented, submitters preferred a definition that would capture listed entities that are majority owned by overseas persons, or where investors with substantial holdings (that is, greater than 5%) cumulatively hold 25% of a class of shares with voting rights.

297. Several submitters proposed an alternate option where listed entities would only be overseas persons if one foreign investor, or group of associated investors, held 25% of its shares. However, this would be inconsistent with the Act’s purpose<sup>50</sup> and would place significant pressure on the OIO’s monitoring and enforcement capability.<sup>51</sup>

298. Submitters also supported exemptions for New Zealand incorporated entities and portfolio investors that are majority owned and controlled by New Zealanders and can demonstrate a strong connection to New Zealand (though there was a view that some of the proposed exemption criteria were unnecessary).<sup>52</sup>

299. There was broad support for no longer requiring investors to gain consent to increase their interest in a sensitive asset if they do not cross a control limit<sup>53</sup>, or to make investments where the acquisition results in the target entity becoming an overseas person.

300. Individual submitters were generally concerned about overseas investment and did not support liberalising the regime, though few commented specifically on these topics.

***We recommend a package of reforms targeted at excluding from the Act:***

- ***fundamentally New Zealand entities; and***
- ***transactions that do not materially change the level of control that overseas persons have over sensitive assets.***

301. We have developed a package of reforms to significantly reduce the number of transactions that require consent (across all categories of sensitive assets) without materially reducing the Government’s ability to manage foreign investment risks. The levels of interdependency within this package mean that it is challenging to present workable alternatives, although we have considered them. If you have concerns with any

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<sup>49</sup> Portfolio investors are entities that generally obtain minority interests in an entity (that is, less than 10%) and have no ability to exert material control over that entity.

<sup>50</sup> The Act’s purpose recognises that it is a privilege for overseas persons to own or control sensitive New Zealand assets. This option would enable 100% foreign ownership with no requirement for consent if all investors were under 25%.

<sup>51</sup> Under this definition it would be relatively easy for associated investors to circumvent the Act. While this would be illegal, it could be difficult for the OIO to detect.

<sup>52</sup> In particular, concern was raised about a proposed requirement that the entity be headquartered in New Zealand and that the entity have received consent previously under the Act.

<sup>53</sup> Control limits are 25, 50, 75% and 100%. A 25% holding allows an investor to block certain special resolutions at a general meeting, a 50% holding allows an investor to pass simple resolutions, a 75% holding allows an investor to pass special resolutions, and 100% is sole ownership.

particular aspect of the package, we can consider how this would affect the overall design and provide further advice.

***Recommended option: narrow definition of “overseas person” for New Zealand incorporated and listed entities***

302. We recommend narrowing the definition of overseas person for bodies corporate incorporated and listed in New Zealand. Listed entities are subject to additional regulatory requirements (e.g. the Financial Markets Conduct Act and NZX listing rules), which mitigate many of the risks associated with ownership or control of sensitive New Zealand assets.<sup>54</sup>
303. Under this proposal, a New Zealand incorporated and listed entity (A) would only be an overseas person where overseas persons:
- a hold 50% or more of A’s total equity securities (the ownership limb); or
  - b with holdings of 10% or more of any class of A’s equity securities cumulatively have:
    - i the power to control the composition of 50% or more of A’s governing body; or
    - ii the right to exercise or control the exercise of more than 25% of the voting power at a meeting of A (the control limb).
304. Under this proposal, entities that are majority owned by overseas persons or realistically subject to control by overseas persons would always be required to obtain consent to acquire sensitive assets (even when they are listed).
305. While we had consulted on a control limb where holdings of 5% (rather than 10%, as now proposed) would be aggregated to 25%, we agree with submitters that this would result in some listed entities being defined as overseas persons even where overseas persons could not realistically exercise control.
306. A 10% aggregation threshold appropriately balances stakeholder concerns against pressures on monitoring and enforcement capability. In addition, adopting this higher threshold ensures that the regime is unlikely to define Mixed Ownership Model companies as overseas persons.<sup>55</sup>
307. This option would have a positive impact on the regime’s predictability and substantially reduce compliance costs for listed entities that are majority owned and controlled by New Zealanders (as they would no longer need to interact with the Act at all). It would also increase New Zealand’s attractiveness to investment because listed entities would be able to attract additional capital before being deemed to be an overseas person, allowing listed entities to invest in New Zealand directly with fewer transaction costs.
308. The proposal would marginally reduce the Government’s ability to manage foreign investment risks. This is principally because the proposed definition (and particularly the 10% aggregation threshold) places more pressure on the OIO’s ability to detect associated investors attempting to circumvent the Act than the current definition. This risk is mitigated by the new definition applying only to listed entities, which are subject to additional regulatory controls.

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<sup>54</sup> For example, listed bodies corporate are required to disclose when a person has a substantial holding (that is, a holding of 5% or more of a class of securities) and any change in that holding of 1% or more. This requirement does not apply to unlisted bodies corporate.

<sup>55</sup> The Public Finance Act prohibits any person (other than the Government) from holding more than 10% of a class of shares or voting securities

***Recommended option: applied-for exemption for New Zealand incorporated companies that are majority owned and controlled by New Zealanders***

310. We recommend allowing New Zealand incorporated (but unlisted) bodies corporate with a strong connection to New Zealand to apply for an exemption from the definition of 'overseas person'. An applied-for exemption is appropriate because non-listed entities are subject to a lower degree of regulatory oversight than listed entities.
311. Consistent with the proposed definition for listed companies, a domestically incorporated (but unlisted) entity would be eligible to apply for an exemption from the definition of overseas person provided it does not meet the ownership limb or the control limb described at paragraph 303, above.
312. Before granting an exemption, the Minister would be required to consider:
- a the level of equity held by a foreign government or its associates (entities in which a foreign government (alone or with its associates) holds 10% or more would not be eligible for the exemption);<sup>56</sup> and
  - b whether the entity has a record of compliance with relevant New Zealand law and the laws of other jurisdictions. This is a proxy for the investor test that applicants must normally satisfy to receive consent under the Act.
313. Exemptions could be made subject to appropriate terms and conditions (for example, maintaining a record of compliance with New Zealand and other jurisdictions' laws). We do not propose that the exemption be time limited. It would remain in place until the relevant entity failed to satisfy the exemption's requirements or breached any conditions imposed.
314. This exemption is expected to have a positive impact on New Zealand's attractiveness to investment by allowing exempted companies to receive additional foreign capital before being deemed an overseas person. It would also significantly reduce the regulatory burden imposed on private companies that are strongly connected to New Zealand. The proposal has no material impact on the Government's ability to manage risks, because fundamentally New Zealand entities are not the regime's targets.
315. Following consultation and further analysis we do not consider that exempted companies should be required to:
- a be headquartered in New Zealand (because the criteria could be easily circumvented and is a superficial indicator of an entity's connection to New Zealand); or
  - b have previously obtained consent under the Act (because this would serve as a barrier to entry and would add little to the general requirement that the entity have a history of compliance with the law).
316. The new exemption will require an amendment to the statutory exemption criteria.

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<sup>56</sup> This reflects the fact that foreign government investors may have strategic, rather than purely commercial, objectives when investing in sensitive New Zealand assets. The 10% threshold is consistent with our broader view of what level of ownership potentially gives rise to control by overseas persons.

317. [1, 36]

***Recommended option: applied-for exemption for managed investment schemes that are majority owned and controlled by New Zealanders***

318. We recommend an exemption targeting managed investment schemes that are majority owned by New Zealanders. We propose limiting the exemption to registered schemes (as defined in the Financial Markets Conduct Act 2013), because they are subject to additional regulatory oversight which mitigates the risks associated with overseas investment.
319. Currently managed investment schemes can fall within the definition of overseas persons even if they are investing predominantly on behalf of New Zealanders – individuals that would not require consent to purchase sensitive assets in their own right. The existing exemptions for portfolio investors and New Zealand controlled entities can no longer be used following changes to the Act in 2018.
320. Under the proposed exemption a managed investment scheme would be eligible for an exemption from the definition of overseas person if:
- a more than 50% of the scheme's funds are invested on behalf of non-overseas persons; and
  - b overseas persons that each hold 10% or more voting power, do not co control more than 25% of voting power at a meeting of scheme participants.
321. In considering an exemption application, consistent with the requirements for New Zealand incorporated companies, the Minister would consider the scheme's compliance with the law and the share of funds derived from foreign governments or their associates. Entities that had received 10% or more of their funds from a foreign government (alone or with its associates) would be ineligible for the exemption.
322. This exemption would improve New Zealand's attractiveness to investment, and have minimal impact on risk management because:
- a investments by managed investment schemes are generally passive and focussed on long term returns rather than exercising control;
  - b the investments are being made primarily on behalf of New Zealanders, who could purchase assets in their own right without consent; and
  - c managed investment schemes are subject to a range of regulatory controls, including reporting obligations and conduct requirements.
323. This exemption would replace the existing exemptions for portfolio investors and New Zealand controlled entities.
324. Exemptions could be made subject to appropriate terms and conditions. However, we do not propose that the exemption would be time limited. It would remain in place until the relevant entity failed to satisfy the exemption's requirements or breached any conditions imposed.

325. [1, 36]

### ***Recommended option: amended class exemption for retirement schemes***

326. Retirement schemes<sup>57</sup> can be defined as overseas persons under the Act – despite being almost exclusively funded by New Zealanders – for a range of technical reasons, such as having a custodian or trustee that is an overseas person.<sup>58</sup> This is despite the fact that scheme participants that are New Zealanders can purchase assets in their own right without obtaining consent and that imposing unnecessary costs on retirement schemes is inconsistent with increasing New Zealanders' retirement savings.

327. Reflecting this, retirement schemes are exempt from consenting requirements where at least 75% of scheme participants are New Zealanders.<sup>59</sup> They are not, however, exempt from the definition of 'overseas person' as we have proposed for qualifying bodies corporate and registered schemes. The consequence of this is that while retirement schemes can purchase sensitive assets without consent, their investments contribute to target entities being deemed to be an overseas person. Given the investors are New Zealanders, this seems inconsistent with the purpose of the Act.

328. To resolve this problem, we recommend amending the existing exemption so that eligible retirement schemes are exempt from the definition of overseas person.

329. This option supports New Zealand's investment attractiveness by allowing retirement schemes to invest in New Zealand entities without a risk of the target entity being deemed to be an overseas person and consequentially subject to additional regulatory costs. Because retirement schemes can already purchase sensitive assets without obtaining consent, this proposal has no effect on the Government's ability to manage risk.

330. [1, 36]

### ***No general exemption for portfolio investors***

331. We consider the proposed exemptions for managed investment schemes and retirement schemes are sufficient to address concerns relating to portfolio investments. We do not propose a general exemption for portfolio investors for the following reasons.

- a Portfolio investors do not usually require consent under the Act (the general trigger for consent is a 25% acquisition, whereas portfolio investors generally acquire interests of less than 10%).
- b The exception is transactions that result in the target entity becoming an overseas person (i.e. transactions that trigger the 'tipping point'). However, under our

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<sup>57</sup> Retirement schemes are defined in Section 6(1) of the Financial Markets Conduct Act 2013. They include Kiwisaver and other superannuation schemes, as well as qualifying workplace savings schemes and single-person self-managed superannuation schemes.

<sup>58</sup> This can often occur because a retirement scheme uses an Australian trustee or custodian to manage and/or direct their funds.

<sup>59</sup> Regulation 44 in the Overseas Investment Regulations 2005.

recommended change to the tipping point, discussed below, portfolio investors will never require consent to invest in New Zealand incorporated and listed entities.<sup>60</sup>

- c Portfolio investors will continue to require consent for investments into non-listed entities if their acquisition results in the recipient entity becoming an overseas person. However, this is not a significant issue because portfolio investors are generally less likely to invest in private entities<sup>61</sup> and the tipping point provisions are less likely to be regularly triggered in private entities than in listed entities, where share ownership can change daily.
- d Investments by (non-exempt) portfolio investors will contribute toward the recipient entity breaching the ownership limb of the definition of overseas person. This limb ensures that an entity will be treated as an overseas person if the majority of economic returns flow offshore. There is no strong rationale for exempting investments by portfolio investors from contributing to this limb.

332. We also recommend repealing the existing exemptions relating to portfolio investors and New Zealand controlled entities. These exemptions can no longer be added to following changes to the Act in 2018, and the proposed changes make them unnecessary.

333. [1, 36]

***Recommended option: no screening for incremental investments where no change in control***

334. Overseas persons are generally required to obtain consent for investments that increase an existing interest of more than 25%. Regulations provide exemptions for some small increases where the overseas person already holds consent.<sup>62</sup> However, our general view is that requiring consent for incremental investments that do not substantially change control imposes an undue burden on reinvestment by overseas persons.

335. We recommend amending the Act so that overseas person only require consent if an investment results in an investor increasing its interest above a control limit (25, 50, 75 and 100%).<sup>63</sup> That is, the investor could move between control bands (e.g. 76% and 99.9%) without obtaining consent. This reflects our view that any increase within a control limit will not substantially change control of a company and therefore will not increase the risks associated with an investment. This change would have a positive impact on New Zealand's attractiveness to investment by reducing barriers to reinvestment.

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<sup>60</sup> This is because only interests of 10% or greater would be used to determine whether a listed bodies corporate is subject to overseas control, and we proposed that the control limb is the only relevant threshold for the tipping point provisions.

<sup>61</sup> Due to, among other factors, the decreased liquidity of their investment.

<sup>62</sup> Under regulation 38, overseas persons that hold consent may increase an existing interest within **five years** of obtaining consent by:

- 5% of the number of securities it initially had consent to hold ('5% limb'); or
- 10% of the number of securities in a class provided that do not exceed a control limit (25, 50, 75, 90% and 100% in this case), ('10% limb').

<sup>63</sup> The current exemption also includes a 90% control limit. We recommend removing this because 10% ownership or control by non-overseas persons carries no substantial value outside of 10% of economic returns flowing to New Zealanders. We do not consider this residual economic benefit justifies the additional compliance burden. The current exemption also includes a 5-year time limit which we also do not consider is required.

336. Our recommended option would also allow overseas persons who invested in a sensitive asset without requiring consent (i.e. the asset was not sensitive at the time of the investment<sup>64</sup>) to increase their investment within the control limits. This would mean that sensitive assets not previously subject to consent requirements would only be brought into the regime when an overseas investor crosses a control threshold. We consider that this position is justified. Imposing consent requirements on investments within control limits is disproportionate to the (minimal) additional risk resulting from those transactions.

337. We recommend this option be incorporated into the Act, and the exemption removed. This would significantly reduce the complexity of the regime.

[1, 36]

[1,36]

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<sup>64</sup> An overseas person could have acquired an interest of 25% or more in sensitive assets without having obtained consent in two ways:

- Amendments to the Act (for example, the 2018 expansion of the Act to cover residential land) mean that consent is now required to acquire the interest in an asset; or
- Changes to the nature of an asset (for example, an interest in a company now worth more than \$100 million was acquired when it was worth less than \$100 million) mean that consent is now required to acquire an interests in that asset.

[1, 36]

**Recommended option: a ‘control-only’ tipping point for New Zealand incorporated and listed entities**

342. Currently investors are required to obtain consent if their investment results in the target entity (which holds sensitive land) becoming an overseas person.<sup>66</sup> The provision is designed to ensure that overseas persons cannot exercise control over sensitive land without obtaining consent.
343. However, the current provision creates significant problems. It requires investors to obtain consent even if their transaction is small and does not grant them any control over sensitive land held by the target entity. This imposes unnecessary costs on investors and can serve as a barrier to investment because it is difficult to demonstrate benefits under the benefits test for small acquisitions. These problems are more significant for overseas persons investing in listed entities because it is more difficult to determine the share of overseas ownership and shareholders can change daily (meaning that the provision could be triggered multiple times per day).
344. To address this problem, we recommend that the tipping point provisions – as they apply to domestically incorporated and listed bodies corporate – be amended to specifically target investments where overseas persons potentially gain control over sensitive assets already held. That is, investors should only require consent if their investment results in the target entity breaching the control limit (rather than the ownership or control limit as occurs currently). Under the proposed package, this would require a minimum investment of 10%.
345. This would increase New Zealand’s attractiveness to investment by reducing the possibility of an overseas person needing to obtain consent without gaining a corresponding chance to control sensitive assets. It would also increase investor certainty, because it will be much simpler to determine when consent is required.<sup>67</sup>
346. This option would not require an investor to obtain consent if their investment results in the ‘ownership limb’ being breached. This could result in sensitive assets acquired by that entity before it was an overseas person becoming 100% foreign owned without any individual overseas person being required to obtain consent. However, this position:
- a is not substantially different to the status quo;<sup>68</sup> and
  - b does not create a material risk because overseas persons would not be able to exercise control over the relevant assets without obtaining consent.
347. [1,36]

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<sup>66</sup> For example, an overseas person acquires 1% of an entity that is already 24% foreign owned.

<sup>67</sup> Holdings of more than 5% in listed entities must be publicly disclosed. This makes it easy to determine whether a prospective investment will breach the control limb. In contrast, it is not possible for investors to easily determine a listed entity’s total level of overseas ownership as required under the status quo.

<sup>68</sup> Currently, the overseas person that acquired the interest that result in an entity becoming an overseas person has to acquire consent regardless of the size of the interest that overseas persons acquires. After consent is given for that investment, no further consent is required from subsequent investors acquiring less than a 25% stake in the target entity irrespective of the overall level of overseas ownership.

### ***Alternative options***

348. While we considered alternative options to address each example of the Act's overreach in terms of the number of entities and transactions it captures, the above package of reforms is designed to work coherently to address the identified problems.
349. If you wish to consider alternative options for any aspect of the package, we will provide further advice (except for the alternative option for incremental investments, which can be accommodated). For example, any change to the proposed control limb (and particularly using 10% as a threshold) for the definition of overseas person for domestically incorporated and listed entities would require us to reconsider our recommendation for the treatment of portfolio investors.