The Treasury

Reform of the Overseas Investment Act Information Release

July 2020

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[4] 6(c) - to avoid prejudice to the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial

[23] 9(2)(a) - to protect the privacy of natural persons, including deceased people

[29] 9(2)(d) - to avoid prejudice to the substantial economic interests of New Zealand

[31] 9(2)(f)(ii) - to maintain the current constitutional conventions protecting collective and individual ministerial responsibility

[33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[36] 9(2)(h) - to maintain legal professional privilege

[37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice

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TE TAI ŌHANGA
THE TREASURY

Treasury Report: Overseas Investment Act Phase 2 Reform: additional policy decisions

Date:	27 August 2019	**Report No:**	T2019/2426
		File Number:	IM-5-3-8 (Overseas Investment Act Phase Two)

Action sought

	Action sought	Deadline
Hon David Parker **Associate Minister of Finance**	**Indicate** your decisions on the following additional policy issues: rural land, the benefits test, special land, incremental investments and managed investment schemes. **Refer** this paper to the Associate Minister of Finance (Hon. David Clark) and the Minister for Land Information.	
Hon Grant Robertson **Minister of Finance**	Note the content of this report	

Contact for telephone discussion (if required)

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

Minister's Office actions (if required)

Return the signed report to Treasury.

Refer this paper to the Associate Minister of Finance (Hon. David Clark) and the Minister for Land Information.

Note any feedback on the quality of the report	

Enclosure: No

Treasury Report: Overseas Investment Act Phase 2 Reform: additional policy decisions

Executive Summary

Purpose

This report seeks your decisions on:

1. *Enshrining the 'rural land directive' in the Overseas Investment Act 2005 (the Act)*: there are several options of differing scopes that could enshrine a higher threshold for investments involving rural land. We recommend retaining the status quo, as options will continue to constrain capital sources that could otherwise support primary sector adaptation to lower-impact land uses, and may lock-in sub-optimal land use. If a reform option is progressed, we recommend the Act makes the presence of farmland an indicator of land's sensitivity, so that an application involving such land must show proportionately higher levels of economic benefit or involvement of New Zealanders in the investment. This option would carry forward the intent and outcomes of the rural land directive, while limiting unintended overreach.

2. *Outstanding decisions relating to the benefits test:* for the types of sensitive land that would not be affected by the rural land proposal, we recommend the screening process should be reformed in the manner outlined in the earlier Treasury report [T2019/1649]: a simplified benefits test and a 'before and after' counterfactual coupled with an explicit proportionate screening approach.

3. *Improving the special land provisions in the Act:* the special land provisions generate substantial compliance costs, delays and uncertainty for all parties involved. We recommend streamlining the process for offering special land to the Crown, removing rivers from the definition of special land, clarifying that the provisions are not mandatory, and confirming that they apply only to the acquisition of freehold interests.

4. *New proposals for incremental changes in shareholding*: there are a range of technical problems with the exemption for small increases in an existing investment. These result in entities being screened for small transactions. The cost of screening is disproportionate to the risk posed by those small transactions.[1]

5. *The definition of overseas person in relation to managed investment schemes*, which would modernise the Act to bring it into line with financial markets legislation.

We are also seeking your decision on new, targeted consultation on the proposals relating to the rural land directive, as they are substantially different from the options consulted on.

These decisions complement the suite of decisions made on the broader package for reform of the Act (T2019/1649 refers).

Additional advice on sensitive adjoining land and the call in power will be provided in late-August/early September. We we are developing timeframes for providing the further advice on tax that you and Minister Clark requested in our meeting on 22 August.

Next steps

You are meeting with us on Thursday 29 August 2019 to discuss this advice.

We recommend you discuss the options with relevant ministerial colleagues (e.g. decision-making ministers under the Act).

Key milestones

The Government has indicated it intends to enact reforms to the Act 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.

Draft Cabinet paper to your office	19 September
Cabinet paper required to be submitted to Cabinet Office	17 October
Cabinet paper at DEV	23 October
Cabinet	29 October

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

[1] We previously recommended an option that would allow entities to increase their interest by any amount between control limits. You disagreed with this option and invited us to make another proposal (T2019/1649 refers).

Recommended Action

We recommend that you:

a **indicate** your decisions on the additional policy issues set out in Table 1 (rural land, the benefits test, special land, incremental investments and managed investment schemes), for inclusion in the draft Cabinet paper on the full package of reforms to the Act;

b **note** that maintaining the status quo is also an option for all issues set out in Table 1;

noted

c **refer** this paper to the Associate Minister of Finance (Hon David Clark) and the Minister for Land Information.

referred / not referred

Megan Noyce
Principal Advisor, International

Hon David Parker
Associate Minister of Finance

Table 1: Summary of recommendations

Issue	Recommended option	Alternative option/s	Minister's comment
How could the rural land directive be enshrined in a reformed screening process? [Section 1]			
You have expressed interest in enshrining the rural land directive in the Act to embed a higher consent threshold for overseas investment in farmland, because of its particularly high economic and cultural value.	Do not enshrine the rural land directive in the Act ***agree/disagree*** **OR** Enshrine the rural land directive in the Act by applying a higher investment threshold to **sensitive land over five hectares that is farmland**, such as land used exclusively or principally for agricultural, horticultural, or pastoral purposes, or for the keeping of bees, poultry, or livestock. Land used principally for forestry would be excluded, as would land that is used for the processing of primary products ***agree/disagree***	Enshrine the rural land directive in the Act by applying a higher investment threshold to land that is **non-urban and over five hectares**, and does not include land used for forestry ***agree/disagree***	
	Provide that the presence of farmland/non-urban land over five hectares (depending on the choice in the recommendation above) is an indicator of land's sensitivity, such that an application must show proportionately higher levels of economic benefit or involvement of New Zealanders in the investment ***agree/disagree*** *This would provide an overlay to the simplified benefit test outlined below*	Where an application involves farmland/non-urban land over five hectares (depending on the choice in the recommendation above), require decision-makers to place high relative importance on factors involving economic benefit and involvement of New Zealanders in the investment, and require that those benefits demonstrate a substantial point of difference ***agree/disagree*** *This would provide an overlay to the simplified benefit test outlined below*	
	If a recommendation to embed the rural land directive is agreed, provide that decision-makers much place high relative importance on a factor relating to the advancement of the Government policies or strategies that relate to sustainability ***agree/disagree***		
	The Treasury should undertake targeted consultation on proposals to embed the rural land directive ***agree/disagree***		

What outstanding decisions about the benefits test are required? (options outlined more fully in the 5 August Treasury report T2019/1649) [Section 2]			
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.	Determine whether investments to acquire sensitive land are of benefit to New Zealand by considering their effect against a: • broad economic factor • broad environmental factor • general public access factor • historic heritage factor • factor relating to advancement of significant Government policies • factor relating to New Zealanders' involvement in the relevant investment, and • factor recognising any other consequential benefits of the investment. Clarify that Ministers cannot consider the negative effects of an investment under this test. Remove the ability to add to this list of factors via Regulations. ***agree/disagree***	The same as the recommended option, but clarify that Ministers can consider the negative effects of an investment on public access under this test. ***agree/disagree***	
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.	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). ***agree/disagree***	**[Alternative]** Determine whether an investment in land is beneficial by considering what is likely to happen if the vendor continues to own it. ***agree/disagree*** **[Alternative or complement]** 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. ***agree/disagree***	
Benefits for investments in non-urban land larger than five hectares must be 'substantial and identifiable'. This will largely duplicate the proposed rural land changes above, and 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.	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. ***agree/disagree***		
How can we improve the special land provisions? [Section 3]			
The special land provisions generate substantial compliance costs, delays and uncertainty for vendors, overseas persons and the Crown. These are primarily caused by difficulties implementing each stage of the offer process:			

– *Notification:* The responsibility for notification – and the rest of the offer process – sits with the vendor, despite it being relevant to whether the overseas person receives consent. This is inconsistent with the treatment of other consent requirements (which sit with the overseas person) and can hold up the consent process.	Amend the Regulations to shift responsibility for notification – as well as the rest of the special land process - from the vendor to the overseas investor. ***agree/disagree***		
– *Right of waiver:* While the Crown may waive its right to acquire the special land at any time after a notice has been given, in practice it rarely executes this right early in the process. This is because the circumstances in which the Crown would seek to accept or waive an offer of special land are not clear.	Amend the Regulations to require the Crown to make an upfront decision, within a certain number of days of notification, about whether to enter into the offer process. ***agree/disagree*** Amend the Act to require the Minister to issue guidance on the circumstances in which the Crown would seek to enter the process to acquire special land. ***agree/disagree***		
– *Surveying:* A survey is required to create a new title and enable transfer of land to the Crown, and may be required for valuation. For riverbed in particular, these can be very complex, time-consuming (3-6 months) and costly. This is because rivers are often located in inaccessible terrain, making it difficult to accurately survey the land in an efficient and effective manner (e.g. large forestry blocks).	Amend the Regulations to require the Crown to decide, as part of its upfront decision, whether it wishes to acquire legal ownership of the special land or an equitable interest only. (Legal ownership requires a full survey, whereas an equitable interest does not). ***agree/disagree***		
– *Valuation:* The Act is unclear as to whether the special land can be gifted to the Crown, avoiding the need to value it. Waterways – especially rivers – are not usually sold, so there is no comparable market on which to base valuations of special land, which makes valuations complex and time-consuming (can take 3-6 months).	Amend the Act to: • provide a process for special land to be offered to the Crown at nil value if the parties chose to do so, and • require a valuation for the special land only if the Crown rejects the offer price. ***agree/disagree*** Request Cabinet to invite the Valuer-General to provide guidance for surveying special land. ***agree/disagree***		
– *Negotiations:* Negotiating terms and conditions can be time-consuming (e.g. 2-4 months for applications under the special forestry test), particularly because they occur between the vendor and the Crown but impact on the investor – who must also be a party to the agreement.	Amend the Act to enable standardised terms and conditions to be set in the Regulations. These would be mandatory unless other agreement was reached with the Crown. ***agree/disagree***		

– *Crown decision:* The Regulations require Ministers to decide whether to accept or waive offers of special land within 30 days of the offer being made. In practice, decisions are taking longer, and the Act is silent on the effect of exceeding the timeframe.	Amend the Regulations so that if the Crown does not make a decision on the offer of special land within the 30 day timeframe, the offer is deemed to be waived. ***agree/disagree*** *Note, the timeframes for making decisions on special land offers would need to be reviewed in line with decisions about the reform of the rest of the special land offer process and the proposed timeframes for deciding consent applications.* ***noted***		
– *Conveyance:* For the Crown to acquire land, it needs to be held under a specific legislative regime and for a specific purpose. The Act is silent on this.	Amend the Act so that where the Crown acquires a freehold interest: • foreshore and seabed offered is transferred to the common marine and coastal area under the MACA Act through the pathways provided for under that Act; and • riverbed and lakebed enters the Crown estate and becomes subject to the Land Act 1948. ***agree/disagree***		
The particular challenges of rivers mean that the cost of surveying them may outweigh the public interest in owning them – particularly as ownership does not guarantee access (which still may need to be negotiated with the owner).	Amend the Act to exclude riverbed from the definition of special land. ***agree/disagree***	As part of guidance on circumstances in which the Crown would seek to enter the process to acquire special land (above), clarify the circumstances in which the Crown would seek to acquire riverbed – e.g. only rivers over a certain size and/or those adjoining conservation land, and not rivers on forestry blocks or farmland. ***agree/disagree***	
It is unclear whether the special land provisions are mandatory or voluntary, as their treatment differs across the Act and Regulations. – In the Act's benefits test, offering special land to the Crown is one of 21 factors that decision makers *may consider* when assessing the benefits of a potential overseas investment in sensitive land, and • In the Act's special forestry test and in the Regulations, offering special land to the Crown is *mandatory*. This causes uncertainty for vendors and investors.	Change the Act and Regulations to clarify that the special land provisions are not mandatory. This would mean: • offering special land to the Crown would remain a non-mandatory factor in the benefits test • offering special land would no longer be a mandatory part of the special forestry test, and • the Regulations would be amended to make it clear that the offer of special land is non-mandatory. ***agree/disagree***	Change the Act and Regulations to clarify that special land is mandatory for foreshore and seabed only. This would mean: • offering foreshore and seabed to the Crown would become a mandatory factor in the benefits test and a mandatory part of the special forestry test • offering riverbed and lakebed to the Crown would remain a non-mandatory factor in the benefits test and would become a non-mandatory part of the special forestry test, and • the Regulations would be amended to reflect these changes. ***agree/disagree***	
The Act provides no guidance on which type of ownership interest the ecial land provisions apply to. [33]	Amend the Act to clarify that special land provisions only apply to the acquisition of freehold interests (either directly or in clear cases of total ownership, such as through using a holding company). ***agree/disagree***		

Are changes need to the incremental investment provisions? [Section 4]			
We consider that the incremental investment provisions are overly restrictive.	*In our previous advice [TR refers], we recommended allowing all incremental investments within control limits (25, 50, 75 or 100%). You disagreed with that recommendation and invited us to formulate an alternative option.* ***noted***		
Small incremental investments by holding companies or subsidiaries of the consent-holder are not eligible for the exemption. This increases compliance cost while only marginally reducing risk because entities were likely screened (as part of the investor test) when the consent-holder initially obtained consent.	Allow overseas persons that have a 25% interest in the consent-holder, or that the consent-holder has a 25% interest in, to increase their interest by any amount less than 10% without requiring consent under the Act. ***agree/disagree***		
Entities that hold an asset before it becomes sensitive and then make small incremental investments after the asset becomes sensitive are required to obtain consent. The compliance cost of screening is disproportionate to the additional risk (if any) those small transactions create.	Allow overseas persons that hold sensitive assets that were not sensitive at the time of acquisition to increase their interest by any amount less than 10% without requiring consent under the Act. ***agree/disagree***		
Entities may only use the exemption within 5 years of the date of consent. The compliance cost of obtaining consent for a small transaction is disproportionate to the additional risk created, particularly given that there are other tools for managing that risk such as ongoing good character conditions for consent.	Remove the five year time limit. ***agree/disagree***		
Entities may not increase their interest above 90% (along with 25%, 50%, 75%) without consent. We do not consider a movement above 90% creates additional risk so the compliance cost of requiring consent in those circumstances is not justified.	Remove the 90% control limit so that overseas persons increase their interest by any amount less than 10%, regardless of whether the 90% control limit is breached. ***agree/disagree*** *There are no control limits in the other limb of the exemption which allows overseas persons to increase their interest 5% of the interest that they have consent to hold.* ***noted***		

Are changes needed to the definition of overseas person to better accommodate managed investment schemes? [Section 5]			
The definition of overseas person does not explicitly refer to managed investment schemes. The issues with this position are as follows: 1. it is inconsistent with New Zealand's financial markets legislation; 2. it results in the OIO spending time determining whether managed investment scheme are captured in the definition of overseas person; 3. it would be inconstant with the language of the exemption for manage investment schemes that we proposed in the earlier Treasury Report [outlined in T2019/1649], which may exacerbate the issue referred to at (2) (i.e. before an entity applies for the exemption they must determine how they are an overseas person).	Include managed investment schemes in the definition of overseas person if: • the manager that is an overseas person; • more than 25% of the value of the scheme's managed investment products are held by overseas persons. ***agree/disagree*** [1, 36] ***noted***		

Section 1: How could the rural land directive be enshrined in a reformed screening process?

1. You have signalled that you wish to enshrine the rural land directive, set out in the Ministerial directive letter, within the Act. We understand your intent is to embed a higher consent threshold for overseas investment in farmland. This would seek to reflect the Government's view that such land has a particularly high economic and cultural value, and that the capability of the New Zealand primary sector makes the case for overseas investment in farmland less compelling.

2. This section considers the implications of the proposal and options to enable it. Time constraints and data gaps have limited analysis of the nature and magnitude of the proposal's impacts, but some considerations are outlined below.

What are the likely implications of the proposal?

Reduction in overseas investment in rural land will continue

3. The options for reform outlined below are expected to continue the outcomes arising under the rural land directive: a substantial reduction in overseas investment in agricultural and pastoral land, and a moderate reduction in overseas investment in horticultural land.[2] Applications would be expected to receive consent where they involved benefits such as conversions to higher value land uses, improvements to the land coupled with significant involvement by New Zealanders, or a highly beneficial development.

4. These options are likely to prevent consent being granted where they would produce only a marginal or incremental improvement in an asset, and make it more difficult for investments involving moderate improvements.

5. Since the introduction of the rural land directive in November 2017, the directive has applied to about 62 percent of sensitive land applications that do not involve residential land, or the intention to reside or special forestry pathways (that is, 76 out of 123 applications).[3] Historically, applications involving rural land have accounted for 75 percent of this type of sensitive land application.[4] The rural land directive is considered to have contributed significantly to this drop.

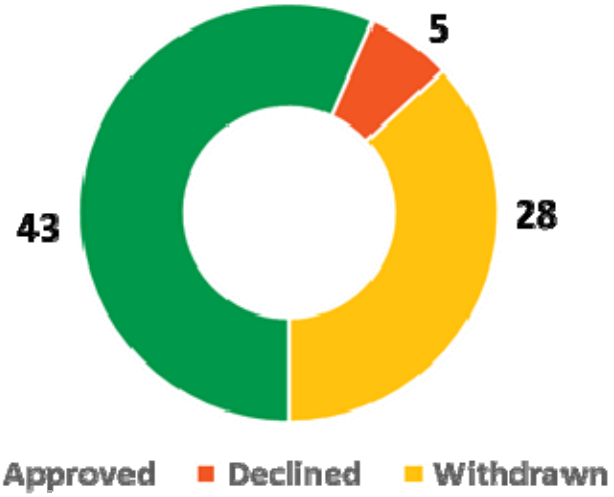
6. About 43 percent of rural land applications have not received consent since the directive was issued, due to applications being withdrawn or declined (see Figure 1 below). The number of withdrawn applications is likely to reflect applicants' lack of familiarity with the change in threshold, rather than a permanent feature of screening under the directive.

[2] As discussed in further detail later in this section, 'rural land' refers to land that is non-urban and over five hectares in size, and does not include land used for forestry. 'Farmland refers tosensitive land over five hectares that is farmland, such as land used exclusively or principally for agricultural, horticultural, or pastoral purposes, or for the keeping of bees, poultry, or livestock.

[3] The remaining 38% of applications comprise land that falls outside the 'rural land' definition (e.g., due to size), applications that have been subject to the forest land directive, or applications to which a directive was dis-applied.

[4] 359 out of 480 over a five year period from 1 July 2014 – 30 June 2019.

Figure 1: Outcomes of applications subject to the rural land directive, December 2017-August 2019



Lower overseas investment will reduce capital available to support primary sector adaptation, and may lock in sub-optimal land use

7. Embedding a reduction in overseas investment risks making it harder for the primary sector to adapt to the range of sustainability-focused reforms currently underway. We do not have a clear picture of the magnitude of the impacts due to the limited time to prepare this advice. The sector is likely to require capital to modify their business models in response to climate, water, and biodiversity-related reforms. Current and potentially forthcoming nutrient discharge limits, for example, will require either a change to current farming systems or a transition to a less impactful land use.

8. At the same time, the main banks argue domestic lending will reduce and/or become more expensive, due to risks in the rural sector (e.g., due to high indebtedness) and the Reserve Bank's proposed new capital requirements for banks. The Reserve Bank notes that the impact of higher bank capital requirements on the agricultural sector is uncertain – the impact will depend on many factors, including banks' target sector allocation, competition, farms' access to other forms of financing, and the transition period for implementing new capital requirements.

9. Constrained resourcing and a reduced pool of investors could make the transition to less impactful land use more challenging, and risk locking in existing sub-optimal land use.

10. Lower overseas investment is likely to lead to lower sale prices for vendors and reduced potential for reinvestment. In cases in which producers are heavily indebted, overseas investment is an option that can help local producers exit and retain some capital for future reinvestment. The Reserve Bank recently noted that a material portion of New Zealand dairy farms have high debt levels that they would struggle to service if their costs rose (as they are expected to in coming months).

11. An elevated benefit threshold could also embed an incentive to convert land to forestry, due to forestry's more permissive screening process. This could come with the risk of

too much afforestation, too quickly and in the wrong areas. This risks unintended effects on the environment and the social licence for forestry activities.

12. Additionally, the proposal could make it more difficult for small investments and transactions involving small shareholding changes to receive consent, due to challenges involved with demonstrating sufficient benefit (proposals later in this report would reduce the risks relating to small shareholding changes).

13. Decision-makers currently have some limited flexibility not to apply the rural land directive when there are clear and persuasive reasons that its intent would not be achieved. For example, the rural land directive has not been applied to a boundary adjustment representing a less than one percent increase in an area of rural land, where the adjustment better reflected current use of land and its natural boundary, and was likely to have environmental benefits. A legislated test will reduce flexibility to accommodate the particular characteristics of individual cases while achieving the certainty required in a legislated test (but the proportionate approach will manage some of the risks).

14. [34]

15. Elements of the reform options respond to the risks relating to adaptation and asset stranding, but are not expected to fully address them.

Perception that overseas investment is not welcome may increase, potentially reducing investment beyond the affected land

16. [1, 34]

[1, 2, 34]

[1, 34]

Recommended Option 1: Retain the status quo

17. We recommend retaining the rural land directive as it currently stands, due to the risks outlined above. However, if an option to enshrine the rural land directive is progressed, we recommend Option 2 below.

Recommended Option 2: Provide that farmland is an automatic indicator of land's additional sensitivity, such that applicants need to show proportionately higher economic benefits

18. Option 2 would require applicants to demonstrate a higher level of benefit when seeking to invest in farmland, relative to other types of land screened under the Act. This would be done by hooking into an existing proposal in the recommended reform package, which involves legislating a proportionate approach to decision-making. The Act would provide that farmland has particular sensitivity, and applicants would therefore be required show a proportionately higher level of benefit to satisfy the benefits test.

19. Consistent with the existing directive, decision-makers would be required to place high relative importance on specified economic benefits, such as new technology or business skills, and the level of New Zealanders' participation in an investment. You could also provide that decision-makers much place high relative importance on a factor relating to the advancement of the Government policies or strategies that relate to sustainability.

20. Decision-makers could still elevate non-economic benefit factors.

21. This option could be slightly more restrictive than the rural land directive in cases involving small assets or small changes in shareholding, as it would not retain the discretion that decision-makers currently have to dis-apply the rural land directive where it would not achieve its policy directive (though the proportionate approach to decision-making would give some flexibility).

22. We are also seeking decisions on options to simplify the counterfactual and benefits test (which were outlined more fully in our earlier report T2019/1649). Consistent with those recommendations, we recommend that a 'before and after' counterfactual and simplified benefits test would apply to transactions affected by a legislated rural land directive. These elements would enable a movement away from the current counterfactual test.

23. Reforming the counterfactual offers potentially greater gains than any other change in the reform package, with one law firm suggesting costs doubled since its introduction. Improved farmland advertising requirements, which you have indicated you wish to adopt, would act to notify potential interested domestic buyers of the sale.

24. Under this option (and Options 3 and 4), the rural land directive would no longer be required.

Alternative option, Option 3: Require decision-makers to place high relative importance on the economic benefit factors, and require these benefits to show a substantial point of difference

25. Option 3 would lift the threshold for investment above that outlined in Option 2. It would require:

    - Decision-makers to place high relative importance on specified economic benefits, the level of New Zealanders' participation in an investment and, if agreed, and any advancement of Government sustainability policy objective, as with Option 2.

- That an application's benefits include either inputs (e.g., technology) or outputs (e.g., increased exports) that are of a size or a nature that represent a substantial point of difference. This would align with the philosophy underpinning the rural land directive – that the New Zealand primary sector is world-leading and only investment that offers some form of compelling value-add should satisfy the benefits test. Defining this threshold with certainty could be challenging, and we would need to work with Parliamentary Council Office on this. Guidance could assist interpretation.

26. As with Option 2, this option would be more restrictive than the rural land directive in certain cases, due to decision-makers' reduced discretion to dis-apply the elevated threshold.

27. To partially mitigate the risk this option could leave vendors with no viable purchaser of an asset, decision-makers could be required to take account of any genuine risk of stranding (that is, there is no New Zealand demand, even at a lower end price).

28. As with Option 2, we recommend that the 'before and after' counterfactual test, simplified benefits test, and proportionate approach in the recommended package would apply.

Range of land affected by proposal

Recommended option: farmland

29. Regardless of whether Option 2 or 3 above is selected, we recommend that the option applies to farmland, defined as sensitive land over five hectares that is farmland, such as land used exclusively or principally for agricultural, horticultural, or pastoral purposes, or for the keeping of bees, poultry, or livestock. Land used principally for forestry would be excluded, as would land that is used for the processing of primary products. Any strategic risks associated with overseas investments in processing plants could be managed through the national interest test.

30. This would focus the proposal on the land that underpins New Zealand's primary sector production, and where we have the strongest evidence of comparative advantage. It would apply the elevated benefit threshold to about 58 percent of sensitive land applications that do not involve residential land, or the intention to reside or the special forestry pathways.

31. This definition would avoid curtailing beneficial investment in areas of primary production in which New Zealand is less internationally competitive. It is narrower than the rural land directive: it would capture about 83 percent of the land currently captured by the rural land directive.

32. This approach would align with the farmland advertising requirement, which also recognises the particular sensitivity of farmland.

Alternative option: non-urban land over five hectares

33. An alternative approach would be to adopt the approach taken in the rural land directive, and apply the proposal to 'rural land' - land that is non-urban and over five hectares in size, and does not include land used for forestry.[5]

34. We would strongly recommend against this approach. Adopting the rural land directive's definition would raise the bar for overseas investment in a less targeted way than the recommended approach. The OIO's experience with the rural land directive indicates this could routinely capture less sensitive non-urban land: it could apply to land on the fringes of cities and towns; large industrial and commercial sites located outside urban areas; significant business assets that are subject to the benefits test due to associated rural land (about 13 percent of applications involve both sensitive land and significant business assets);[6] sites of extractive industry; sites for infrastructure (like power stations); and primary processing sites like sawmills. It is difficult to argue that New Zealand has a comparative advantage in all of these industries.

Need to refine the definition of affected land

35. Regardless of whether Option 2 or 3 is chosen, we would undertake additional work to define the parameters of the affected land more precisely. This may be achieved through District Valuation Roll categories, which would precisely delineate affected land and lessen the risk of unintended overreach, as the categories are based on highest and best use of the land.

Ensuring consistency with international obligations

36. [1, 36]

[5] The rural directive's definition was selected as it aligned with the land type that triggers the 'substantial and identifiable' benefit threshold in the Act, and was intended to cover some categories beyond farmland – such as lifestyle blocks and islands (the residential provision in the Act now deals with the former).
[6] Types of application made under the Act (June 2013 to August 2018).

Options analysis - comparison with the status quo, under which the Act and rural land directive apply

Options	***Impact summary***		
	Manages the risks of overseas investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
***Recommended option*:** **Option 1:** Maintain the status quo	**Neutral**	**Neutral**	**Neutral**
OR ***Recommended option*:** **Option 2:** Provide that the presence of farmland is an indicator of land's sensitivity, such that that an application must show proportionately higher levels of economic benefit or involvement of New Zealanders in the investment	**Neutral** Would continue to require greater benefits for investments in farmland. Would continue emphasise economic benefit factors and New Zealanders' participation in the investment While this option would cover a narrower range of land than the directive, it would target farmland, consistent with the policy intent. Could incentivise investments in short-term leases that are not screened.	**Neutral** While the requirement for greater benefits would be continued, it would target a narrower type of land. The impact of narrowing the type of land captured is likely to be offset by an increased risk of unintended overreach, as this option would not carry forward the limited flexibility decision-makers have to dis-apply the rural land directive (though the proportionate approach would give some flexibility).	**Neutral** No material change expected.
Alternative: **Option 3:** Where an application involves farmland, require decision-makers to place high relative importance on the economic benefit factors, and require those benefits include an input or output that shows a substantial point of difference	**Neutral** As above. Additionally, would more explicitly require benefits to be of a substantial nature.	**Moderately negative** Embeds a higher bar for investment. Applicants would need to show a substantial point of difference in their intended land use – such as diversification of land use or a change to higher value use. While this option would target a narrower type of land than the directive, it would have a substantially higher risk of unintended overreach, as a result of a high benefit threshold and absence of decision-makers current limited flexibility to dis-apply the rural land directive (though the proportionate approach would give some flexibility).	**Moderately negative** Greater uncertainty and compliance burden as it would introduce a new, higher threshold that is unlikely to be precisely defined
Alternative: **Option 4:** Apply either Option 2 or 3 to non-urban land over five hectares	**Neutral** Broader definition of affected land is not expected to provide additional ability to manage risk.	**Strongly negative** In addition to the impacts outlined above, this option would apply to a broader range of land types where it is difficult to argue that New Zealand has a comparative advantage.	**Moderately negative** As above.

Progressing changes and impact on reform package

37. We recommend additional, targeted consultation because the options outlined above (particularly Option 3) are markedly different from the options on which we consulted. This would create a risk to our ability to prepare a Cabinet paper for policy decisions in October.

38. Consultation should include primary industry leaders and iwi, given the potential impact on Māori interests. As Māori land is largely rural, the proposal may disproportionately affect Māori commercial interests, and may be regarded as adding barriers to the use of settlement redress. There are likely to be difficulties organising iwi consultation at short notice, though this can be mitigated by undertaking targeted consultation.

39. Some further work will also be required to confirm the scope of key definitions (particularly the boundaries of land within scope of the proposal), and our experience with the forestry pathway indicates the complexity of integrating a tailored screening process for a particular land use into the Act. [36]

Section 2: What outstanding decisions about the benefits test are required?

40. For the types of sensitive land that would not be affected by the proposals above relating to the rural land directive,[7] we recommend the screening process should be reformed in the manner outlined in our earlier Treasury report [T2019/1649]: a simplified benefits test and a 'before and after' counterfactual, coupled with an explicit proportionate screening approach.

Options analysis

Options	***Impact summary***		
	Manages the risks of investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
Recommended options: Introduce a simplified benefits test with national interest 'backstop' test for higher-risk applications.	Strongly positive	Moderately positive	Moderately negative
Replace current counterfactual with a 'before and after' test that compares the applicant's plans with the state of the land at the time of the application.	Moderately negative	Moderately positive	Moderately positive
Introduce a legislative requirement that benefits must be proportionate to the sensitivity of the land and remove the 'substantial and identifiable' benefit threshold.	Moderately positive	Neutral	Moderately positive
Alternative options: Introduce a 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
Replace the current counterfactual with a comparison of the applicant's plans with 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

[7] Remaining types are:

- any residual types of non-urban land that are not caught by the options discussed in this paper
- land over 0.4 ha on specified islands
- land of any size on other islands (excluding the North and South Islands)
- foreshore or seabed of any size
- beds of lakes over 0.4 ha
- land over 0.4 ha held for conservation purposes
- land over 0.4 ha that a district plan or proposed district plan under the Resource Management Act 1991 provides is to be used as a reserve, as a public park, for recreation purposes, or as open space
- land over 0.4 ha subject to a heritage order, or a requirement for a heritage order, under the Resource Management Act 1991 or by Heritage New Zealand Pouhere Taonga under the Heritage New Zealand Pouhere Taonga Act 2014
- a historic place, historic area, wahi tapu, or wahi tapu area over 0.4 ha that is entered on the New Zealand Heritage List/Rārangi Kōrero or for which there is an application that is notified under the Heritage New Zealand Pouhere Taonga Act 2014
- sensitive adjoining land.

41. Special land is qualifying foreshore, seabed, riverbed or lakebed.[8] The practice of offering special land to the Crown was introduced with the 2005 Act. It reflects the concept of 'ownership value': that is, that some New Zealanders derive a welfare benefit from knowing that certain types of land are owned and controlled by New Zealanders (in this case, the Crown). However, it is important to note that ownership of special land does not guarantee the Crown or public access to that land.

42. Offering special land to the Crown is a factor in the benefits test and a requirement under the new special test relating to forestry activities (the 'special forestry test'). The offer process involves:

Notification	The owner must give written notice to the Crown that a proposed overseas investment transaction includes special land (Regulations 13 and 14).
Right of waiver	The Crown may waive its right to acquire the special land under Regulation 15 at any time after a notice has been given and before a final agreement is entered into.
Surveying	If the Crown chooses not to waive its right to acquire the special land, the land is surveyed and valued according to the procedure set out in Regulations 16 - 21. The Crown pays for the survey where required and, in conjunction with the owner, appoints a public valuer for the valuation.
Valuation	
Negotiation	Under Regulation 22, the owner and the Crown must negotiate in good faith an agreement in principle to the terms and conditions of the acquisition. If this is successful, the owner must offer the special land on the terms and conditions in that agreement. At this point the special land factor has been satisfied (Regulation 23).
Crown decision	Under Regulation 24 the Crown must decide whether to accept or waive the offer within 30 working days of receiving it from the owner. Acquisition by the Crown is conditional on consent being granted and the investment transaction taking place (Regulation 25).
Conveyance	If the offer is accepted, the special land is conveyed to the Crown. This step does not need to be completed prior to the consent process proceeding.

43. Approximately 16 per cent of sensitive land applications in the past five years have involved special land (totalling approximately 20 applications per year), as have 75 per cent of forestry applications under the special forestry test since it was introduced in October 2018 (because land suitable for forestry tends to also contain waterways).

The special land provisions are not working

44. The special land provisions generate substantial compliance costs, delays and uncertainty for vendors, overseas persons and the Crown. The impact of these issues means that the Crown:

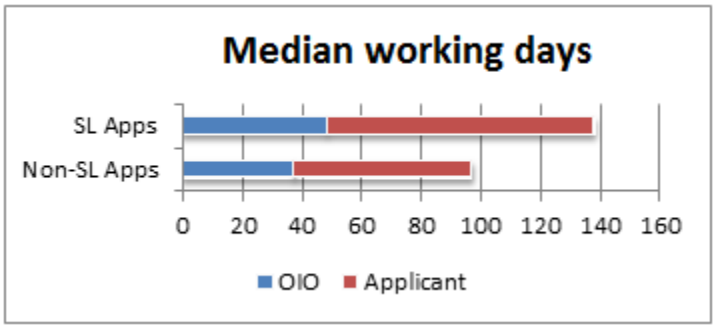
[8] The Act defines rivers and lakes for the purpose of special land as below:

- Lake means a lake (as defined in section 2(1) of the Resource Management Act 1991) that has a bed that exceeds 8 hectares in area.
- River means a river (as defined in section 2(1) of the Resource Management Act 1991) that has a bed of an average width, for its length on or adjoining the relevant land, of 3 metres or more. (Note that special land does not include beds of 'navigable' rivers or those subject to tidal flow, which are already considered Crown land.)

- Has acquired an equitable interest in only three areas of special land since the provisions were introduced in 2005, and has never acquired legal ownership.[37]

- Has negotiated agreements in principle to acquire all special land it has been offered since the introduction of the current Ministerial Directive Letter on 28 November 2017, but has proceeded to a decision on only one.

45. The issues with the special land provisions are also causing significant delays for applications going through the special forestry test, in which timeframes for applications with special land are around 40 percent higher than for those without:[10]



46. Moreover, because the requirement to offer special land must occur before each piece of land is acquired, it is incompatible with the special forestry test's standing consent option (the purpose of which is to speed up the consent process by allowing an applicant to acquire land without first having to meet consent criteria).

47. The primary drivers of cost, delay and uncertainty in the special land provisions arise from difficulties implementing the offer process itself – particularly when an offer involves riverbed.

48. A secondary issue is ambiguity about the status of the special land provisions, as whether they are mandatory or voluntary differs across the Act and Regulations. This ambiguity generates uncertainty.

Difficulties implementing the offer process

Notification	The responsibility for notification – and the rest of the offer process – sits with the vendor, despite it being relevant to whether the overseas person receives consent. This is inconsistent with the treatment of other consent requirements (which sit with the overseas person), and can hold up the consent process.
Right of waiver	While the Crown may waive its right to acquire the special land at any time after a notice has been given, in practice it rarely executes this right early in the process. This is because the circumstances in which the Crown would seek to accept or waive an offer of special land are not clear. While the most recent Ministerial directive letter states that the Government's general policy approach is to acquire special land if it is in the public interest to do so, there is

[37] s

[10] These figures are not reflected in the OIO's reporting on timeframes, which only counts OIO working days.

	no guidance on determining public interest.
Surveying	A survey is required to create a new title and enable transfer of land to the Crown, and may be required for valuation. For riverbed in particular, these can be very complex, time-consuming (3 - 6 months) and costly. This is because rivers are often located in inaccessible terrain, making it difficult to accurately survey the land in an efficient and effective manner (e.g. large forestry blocks). Surveys are not required if the Crown chooses to take an equitable interest rather than legal ownership (i.e. an 'option' to buy the land at a point in the future. This does not provide the same rights as ownership, e.g. any access requirements would still need to be negotiated with the legal owner). While the regulations require the Crown to pay for the survey, no funding is provided for this purpose.
Valuation	The Act is unclear as to whether the special land can be gifted to the Crown, avoiding the need to value it. Waterways – especially rivers – are not usually sold, so there is no comparable market on which to base valuations of special land, which makes valuations complex and time-consuming (can take 3 - 6 months).
Negotiation	Negotiations typically cover matters such as price, liabilities (including for rates, fencing, weeding and maintenance) and access provisions (for Crown, public or applicant). Negotiating terms and conditions can be time-consuming (e.g. 2 - 4 months for applications under the special forestry test), particularly because they occur between the vendor and the Crown but impact on the investor - who must also be a party to the agreement.
Crown decision	The Regulations require Ministers to decide whether to accept or waive offers of special land within 30 days of the offer being made. In practice, decisions are taking longer, and the Act is silent on the effect of exceeding the timeframe.
Conveyance	For the Crown to acquire land, it needs to be held under a specific legislative regime and for a specific purpose. The Act is silent on this.

Ambiguity about the status of the special land provisions

49. It is unclear whether the special land provisions are mandatory or voluntary, as their treatment differs across the Act and Regulations:

    - in the Act's benefits test, an offer of special land to the Crown is one of 21 factors that decision makers *may consider* when assessing the benefits of a potential overseas investment in sensitive land, but

    - in the Act's special forestry test and in the Regulations, offering special land to the Crown is *mandatory*.

50. [36]

    More broadly, continuing to treat the special land provisions as mandatory risks undermining the overall objectives of the current review of the Act, as well as other proposals for reform (e.g. those around introducing statutory timeframes). While we

are proposing steps to improve the process (below), the extent of possible efficiency gains remains unclear at this stage.

Recommended Option 1: Streamline the offer process

Notification	We recommend amending the Regulations to shift responsibility for notification – as well as the rest of the special land process - from the vendor to the overseas investor. This will make the special land provisions consistent with other consent requirements in the Act and Regulations, which will improve certainty for vendors and investors.
Right of waiver	We recommend amending the Regulations to require the Crown to make an upfront decision, within a certain number of days of notification, about whether to enter into the offer process. We also recommend amending the Act to require the Minister to issue guidance on the circumstances in which the Crown would seek to enter the process to acquire special land.
Surveying	We recommend, as part of its upfront decision (above), that the Crown decide the type of ownership interest it wishes to acquire (e.g. legal ownership or equitable interest only). Full legal ownership requires a full survey process, while registering an equitable interest does not require a survey (though one would still be required if the Crown chose to exercise its right to negotiate legal ownership).
Valuation	We recommend amending the Act to: • provide a process for special land to be offered to the Crown at nil value if the parties chose to do so [1,36] • require a valuation for the special land only if the Crown rejects the offer price. Additionally we recommend that Cabinet invite the Valuer-General to provide guidance for surveying special land.
Negotiation	We recommend amending the Act to enable standardised terms and conditions to be set in Regulations. These would be mandatory unless other agreement was reached with the Crown. Examples of standardised terms and conditions appear in section 111 of the Land Act 1948. This approach would enable transparency about the starting point for negotiations on key aspects such as access (for investor or Crown) and contribute towards consistency of agreements. It would also contribute to improving the efficiency of the process.
Crown decision	We recommend amending the Regulations so that if the Crown does not make a decision on the offer of special land within the 30 day timeframe, the offer is deemed to be waived. This would improve certainty for both vendors and investors. Note that the timeframes for making decisions on special land offers would need to be reviewed in line with decisions about the reform of the rest of the offer process and the

[1,36]

	proposed timeframes for deciding consent applications.
Conveyance	We recommend amending the Act so that where the Crown acquires a freehold interest: • foreshore and seabed offered is transferred to the common marine and coastal area under the MACA Act through the pathways provided for under that Act; and • riverbed and lakebed enters the Crown estate and becomes subject to the Land Act 1948.

Recommended Option 2: Remove riverbed from the definition of special land

51. Given the particular challenges of rivers, the cost of surveying and purchasing them may outweigh the public interest in owning them – particularly as ownership does not automatically guarantee access (which still may need to be negotiated with the owner). For this reason, we recommend revising the definition of special land to exclude riverbed.

52. However, if you wish to maintain riverbed in the definition of special land, we recommend using guidance (discussed above) to clarify the circumstances in which the Crown would seek to acquire riverbed. This could state, for example, that the Crown was only interested in rivers over a certain size and/or those adjoining conservation land, and is not interested in rivers on forestry blocks or farmland (if this is the case). We also recommend making the offer of riverbed non-mandatory (discussed further below).

Recommended Option 3: Clarify that the special land provisions are not mandatory

53. We recommend removing the ambiguity in the Act and Regulations by clarifying that the special land provisions are not mandatory. This would mean:

    - offering special land to the Crown would remain a non-mandatory factor in the benefits test

    - offering special land would no longer be a mandatory part of the special forestry test, and

    - the Regulations would be amended to make it clear that the offer of special land is non-mandatory.

54. Under this option, there is a risk that applicants would choose not to offer special land to the Crown due to the complexity of the offer process, which may mean the Crown would miss acquiring special land that was of public interest. However, we think this could be mitigated by providing direction (via the Ministerial Directive Letter) about weighting of this factor.

55. As an alternative, we would recommend making the offer of special land mandatory for foreshore and seabed only. Doing so would reflect the ownership value of this land, which has been reinforced since the Act was introduced by the Marine and Coastal Area (Takuitai Moana) Act 2011 (MACA). This approach would mean:

    - offering foreshore and seabed to the Crown would become a mandatory factor in the benefits test and a mandatory part of the special forestry test

- offering riverbed and lakebed to the Crown would remain a non-mandatory factor in the benefits test and would become a non-mandatory part of the special forestry test, and

- the Regulations would be amended to reflect these changes.

Recommended Option 4 (technical change): Clarify that the special land provisions apply only to freehold transactions

56. The Act provides no guidance which type of ownership interest the special land provisions apply to. In practice, the OIO has taken the view that the special land provisions do not apply where an interest less than a freehold interest is being acquired (e.g. a leasehold interest), and where the interest being acquired is not a direct interest in special land (e.g. shares in a company which has an interest in special land).

57. We recommend amending the Act to clarify that special land provisions apply only to the acquisition of freehold interests (either directly or in clear cases of total ownership, such as through using a holding company).

58. Submitters supported a clarification to provide more predictability as to when the special land provisions apply, though did not expect it to have much practical impact as it reflects current practice.

Options analysis – comparison with the status quo

Options	***Impact summary***		
	Manages the risks of overseas investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
Recommended option 1: streamline the offer process.	Neutral	Strongly positive	Strongly positive
Recommended option 2: remove riverbed from the definition of special land.	Moderately negative	Strongly positive	Strongly positive
Alternative option 2: use guidance to clarify the circumstances in which the Crown would seek to acquire riverbed.	Neutral	Moderately positive	Moderately positive
Recommended option 3: clarify that the special land provisions are not mandatory.	Strongly negative	Strongly positive	Strongly positive
Alternative option 3: make special land provisions mandatory for foreshore and seabed only.	Moderately negative	Moderately positive	Moderately positive
Recommended Option 4 (technical change): clarify that the special land provisions apply only to freehold transactions.	Neutral	Moderately positive	Moderately positive

Section 4: Are changes needed to the incremental investment provisions?

59. Our 5 August 2019 report [T2019/1649] recommended allowing incremental investments within control limits (25, 50, 75 or 100%). You disagreed with that recommendation and invited officials to formulate an alternative option.

60. Our April consultation document sought feedback on a range of technical amendments that could improve the existing exemptions for small incremental investments (that is, small increases after an entity already has 25% or more interest). There was broad agreement amongst submitters with the problems and solutions identified. Submitters also identified the 90% control limit as an additional problem.

61. The Act screens a transaction where an overseas person makes additional incremental investments (directly or indirectly) in a sensitive asset, for which they already have consent to hold.

62. The Overseas Investment Regulations exempt some small incremental investments that do not materially change an investor's control of sensitive New Zealand assets. This reflects the view that the cost of obtaining consent is disproportionate to the additional risk created by these transactions.

63. Broadly, the existing exemption applies if:

    a a person has consent to hold shares in the target company

    b the securities being acquired are of the same class as those which the overseas person has consent to hold;

    c the investment is either:

        i less than 5% of the total number of shares for which the overseas person initially had consent ('5% limb'), or

        ii not more than 10% of all shares in the class and does not result in the overseas person crossing a control threshold (25, 50, 75, 90% and 100%) ('10% limb), and

    d the investment occurs within five years of the overseas person getting consent.

Technical problems with the exemption mean low risk transactions are subject to screening

64. A range of technical problems lead to small increases in shareholding having to be screened. These small transaction have minimal risk associated with them.

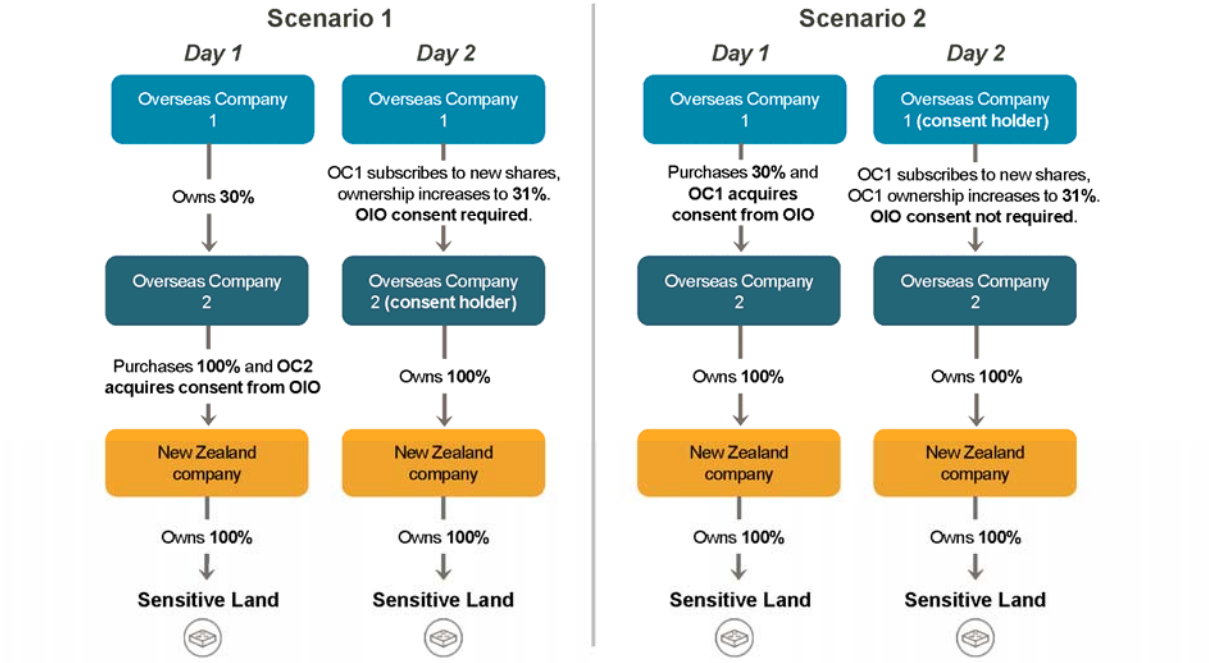
65. The cost of obtaining consent is discouraging overseas persons from increasing their interest in sensitive assets by small amounts. This limits New Zealand's ability to attract long-term investment. It is also likely that entities are unknowingly breaching the Act by not obtaining consent for small transactions (particularly 'upstream' transactions outside of New Zealand). These views were reiterated by submitter and stakeholders during consultation.

66. The technical problems with the current exemption and the recommended solution to resolve them are set out below.

Holding companies and subsidiaries of the consent-holder cannot use the exemption

67. The exemption applies only to an overseas person that already holds consent. This means that if a holding company or subsidiary entity increases its interest in a sensitive asset (directly or indirectly), it will be required to get consent, even though that entity would have been subject to screening as part of the initial transaction for which consent was obtained. During consultation submitters, including NZX Limited, agreed that this was a problem.

68. The problem is illustrated in the diagram and accompanying text below:



69. Scenario 1 and scenario 2 are fundamentally the same except that a different company holds the consent (overseas company 2 in scenario 1; overseas company 1, in scenario 2). This means that in scenario 1 the transaction on day 2 requires consent, while in scenario 2 it is exempt. This is despite the fact that the board of the overseas company 1 would most likely be screened under the investor test as part of the initial consent (and be subject ongoing good character conditions) in both cases.[12]

70. The transactions in scenario 1 and scenario 2 are not materially different in terms of risk, and treating them differently decreases New Zealand's attractiveness to long-term investment.

[12] Our recommended option to expand the good character test to include corporate character will mean that overseas company 1, rather than just its board or natural person shareholders, will also be screened and subject to conditions.

Recommended Option 1: Allow entities with a 25% interest in the consent-holder, and entities which the consent-holder has a 25% interest in, to use the exemption

71. We recommend allowing any 25% upstream or downstream interest-holder in the entity that holds consent to use the exemption (e.g. 25% shareholder consent-holder or an entity which the consent-holder is 25% shareholder in). This would address the problem identified and would not materially reduce the Government's ability to manage investment.

Overseas persons that acquired an asset before the asset becomes sensitive cannot use the exemption

72. The exemption does not apply to a transaction if the asset was not sensitive when the overseas company initially acquired its interest. An asset can become sensitive over time if:

- there is a law change or regulatory change, for example a rating category of land changes to residential or a neighbouring property becomes a reserve, or
- a change to the asset's nature makes the asset sensitive, e.g. an increase in the value of a company (to more than $100 million) makes shares in the company become 'significant business assets'.

73. The OIO advises that this issue has been particularly pronounced for the accommodation industry. This is because hotels are often on residentially-zoned land so consent is required for small increases in shareholding (e.g. [27] often require consent for small changes in its upstream shareholding). The compliance cost of screening these transactions is disproportionate to the marginal increase in the Government's ability to manage risk (the decision-maker can decline consent only for the small increase and cannot make the investor sell down its interest).

Recommended Option 2: Make overseas persons who acquired a sensitive asset before it became sensitive eligible for the exemption

74. We recommend amending the exemption so that an entity is not required to hold consent to be eligible for the exemption, if:

- consent was not required at the time of the initial transaction; and
- the initial transaction would require consent if it were to occur today (because the underlying asset has become sensitive since the original transaction).

75. On its face, this option reduces the Government's ability to manage the risk of investments, because it would remove the ability to subject overseas persons to screening (where screening was not required for the initial transaction). However, an overseas person is already allowed to maintain its interest in a sensitive asset even if an application to increase in its interest is declined. We do not consider this option materially reduces the Government's ability to manage risk when compared with the

status quo (maintaining its interest) given that material increases (over 10%) would still be screened.

Overseas persons can only use the exemption within five years of the date of consent

76. The five year time limit is designed to reduce the likelihood of an overseas person changing in character or composition over time such that they would no longer pass the investor test. We consider that this risk is addressed by the OIO's ongoing good character conditions, which require ongoing satisfaction of the good character criteria (and breach of which results in enforcement action).

Recommendation Option 3: Remove the five year time limit

77. We recommend removing the five year time limit on the exemption.

78. If you are not in favour of removing the time limit, then it could be extended, but we have been unable identify a length of time that is not arbitrary.

Overseas persons are required to get consent if they increase their interest over the 90% control limit

79. The 10% limb of the exemption requires overseas persons to get consent if they cross 90% interest. The 90% control limit does not increase the Government's ability to manage risk because the holder of the remaining 10% does not have any ability to exert substantial control over the sensitive asset.

Recommended Option 4: Remove the 90% control limit

80. We recommend removing the 90% control limit. The (minimal) value in maintaining the residual 10% of New Zealand ownership is disproportionate to the compliance cost of an investor being required to go through screening to increase above 90%

Options analysis - comparison with the status quo under the exemption

Options	***Impact summary***		
	Manages the risks of overseas investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
Recommended option 1: allow overseas persons that have a 25% interest in the consent-holder, or that the consent-holder has a 25% interest in, to increase their interest by any amount up to 10%.	Neutral	Moderately positive	Moderately positive
Recommended option 2: allow overseas persons that hold sensitive assets that were not sensitive at the time of acquisition to increase their interest by any amount up to 10%.	Neutral	Moderately positive	Moderately positive

Recommended option 3: remove the time limit on incremental investments.	Neutral	Moderately positive	Moderately positive
Recommended option 4: remove the 90% control limit so that overseas persons can make incremental investments over the 90% control limit without consent.	Neutral	Moderately positive	Moderately positive

Section 5: Are changes needed to the definition of overseas person to better accommodate managed investment schemes?

81. In the earlier Treasury Report [T2019/1649], we recommended an exemption from the definition of overseas person, that 'fundamentally' New Zealand-managed investment schemes could apply for (MIS exemption). You agreed with our recommendation. This section recommends minor changes to the definition of overseas person to modernise the Act and ensure that the definition of overseas person reflects the proposed exemption.

82. The definition of overseas person does not currently refer to 'managed investment schemes', as that concept post-dates the Act.[13] Managed investment schemes are likely caught either through their manager or as unit trusts (which are no longer[14] used in New Zealand), trusts or the catch-all for unincorporated bodies corporate. [34] There is a chance that this issue may be exacerbated by the MIS exemption (which will introduce managed investment schemes as a concept to the Act).

Recommended option: Include managed investment schemes in the definition of overseas person

83. We recommend amending the Act so that it expressly refers to managed investment schemes in the definition of overseas person. Under this proposal, a managed investment scheme would be an overseas person if:

- the manager is an overseas person, or
- more than 25% of the value of the scheme's managed investment products is held by overseas persons.

84. This would modernise the Act to reflect current financial markets law, reduce the complexity of the regime and may marginally reduce compliance costs. It would also ensure that the definition of overseas person is consistent with the proposed exemption for managed investment schemes you agreed to in the earlier Treasury Report [T2019/1649]

85. [1, 36]

[13] Managed investment schemes were introduced to New Zealand financial markets law under the Financial Markets Conduct Act 2013.

[14] We do not recommend removing unit trusts from the definition of overseas person because they are still used in other jurisdictions.

Options analysis – comparison with the current treatment of managed investment schemes

Options	***Impact summary***		
	Manages the risks of investment	Supports overseas investment in productive assets	Encourages more predictable, transparent and timely outcomes
Recommended option*:* amend the definition of overseas person to include managed investment schemes in which: • the manager is an overseas person, or • more than 25% of the value of the scheme's managed investment products is held by overseas persons.	Neutral	Neutral	Neutral/ Moderately positive

Departmental comment section

86. We consulted 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 Department of Conservation (DOC) and Crown Law.

87. Our recommendations reflect the need to take a broad view of how best to support overseas investment while managing its risks.

88. The OIO were supportive of the proposed changes to the incremental investment regime and the inclusion of managed investment schemes in the definition of overseas person.

89. DOC did not agree with the recommendation to remove riverbed from the definition of sensitive land as it considers the acquisition of riverbed can deliver high benefits to the public and biodiversity management. DOC also disagreed with the recommendation to clarify that the special land provisions apply only to freehold transactions, as notes that some leases can have a similar character to freehold land (e.g. a perpetually renewable lease) or can provide similar benefits to the owner (e.g. a 60 year lease).

90. TPK repeated concerns expressed in relation to the broader reform package 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. It considers that further consultation could enable these further matters to be considered. These issues are outside the Terms of Reference.