New Zealand Law Society
Te Kāhui Ture o Aotearoa

Overseas Investment Amendment Bill (No 3)

12/08/2020

Submission on the Overseas Investment Amendment Bill (No 3)

Introduction

1. The New Zealand Law Society | Te Kāhui Ture o Aotearoa (**Law Society**) welcomes the opportunity to comment on the Overseas Investment Amendment Bill (No 3) (**Bill**). The Bill amends the Overseas Investment Act 2005 (**principal Act**) and is one of two bills which are to replace the Overseas Investment Amendment Bill (No 2).
2. The Bill has been considered by property law practitioners in the Law Society's Property Law Section with assistance from external practitioners experienced in Overseas Investment Office (**OIO**) matters.
3. This submission identifies:
   3.1. the additional layer of complexity the Bill will add to the principal Act;
   3.2. provisions that may create unintended consequences, where further review should be considered; and
   3.3. areas of uncertainty.
4. The Law Society does not wish to be heard but is happy to discuss its comments with the select committee or officials if that would be of assistance.

General comments

5. The principal Act has become very complex and difficult for practitioners to apply and advise on, due to recent amendments.[1] The Bill will add to the intricacies of the consent and notification requirements in the principal Act. Applications, particularly for sensitive land consents, will require a high degree of expertise and effort to meet the exacting requirements of the Act and the OIO. These types of applications are likely to come at a significant cost and may limit the ability for small and medium enterprises and individuals to undertake investments, resulting in New Zealand losing out of the benefits that may otherwise have been provided. Compliance with the principal Act will also become more complex for practitioners.
6. The use of and addition of schedules containing key provisions and further provisions located in regulations makes access to information on the regime very convoluted for practitioners, and extremely difficult for the general public to follow the rules and requirements. It is respectfully suggested a fresh approach to the principal Act is urgently required, rather than continuing to make piecemeal amendments to the now outdated structure.

Proposed amendments to section 7 of the principal Act – clause 5

Amendment to the definition of who is an "Overseas Person"

Listed Companies

7. The proposal to exclude "fundamentally New Zealand entities" from the definition of Overseas Person is supported in principle.

[1] Including the 2018 amendments to include residential property, and the recent Overseas Investment (Urgent Measures) Amendment Bill relating to commercial transactions.

8. However, a practical issue with implementation is the continued reference to overseas persons having a percentage beneficial entitlement to or interest in the entities' securities. For example, it is difficult to determine if any shareholder of a listed company is an overseas person at any given time, especially in situations where shares are traded regularly or where shares are held by trustees (which could be held for overseas persons or for New Zealand persons) .

9. The inclusion of 'associates' loads an extra requirement onto listed companies. The presence or otherwise of associates will be difficult, if not impossible, to detect by the listed company at the time its shares are traded. It is uncertain whether the reference to associates under the control test, and not the ownership test, will result in an interpretation that associates can be excluded under the ownership test.

10. An unintended consequence may be that listed companies which are close to the 50% overseas shareholding may take a prudent approach of either unnecessarily making applications for consent for its purchases of sensitive (including residential) land, or not proceeding with the purchase at all. Making an application presents a significant barrier to carrying on business.

Trusts

11. The 2018 amendments to include residential property as sensitive land has created practical issues with land held by family trusts. The slight amendment to the definition in the Bill does not address those practical issues.

12. Family trusts are widely used to hold property and to lend money to beneficiaries to purchase property. Long term residents in New Zealand who are not citizens can (and do) set up trusts to protect family assets for themselves and their children. By not being a citizen, if a parent who is a trustee or has certain controls over the trust is absent from New Zealand for over six months, the trust is deemed to be an overseas person and cannot purchase or take security over residential properties. Often then there are no consent pathways available under the Act. Reorganisation of family affairs is consequently prevented—for example, for estate planning purposes, or moving ownership from, say, a family trust to direct ownership by a beneficiary who is technically an overseas person because they happen to be working in Australia for more than 6 months.

13. It is recommended that a simple exemption pathway be created to deal with these types of innocuous transactions involving residential land.

Proposed amendments to section 12 of the principal Act – clause 6

Amending what are overseas investments in sensitive land

14. Clause 6 provides for leases which would require OIO consent in the following circumstances:

    14.1. where the land is residential, a lease for 3 years or more unless it is an exempted interest; or

    14.2. where the land is sensitive (but not residential) if the lease is for 10 years or more.

15. The proposed amendment to section 12(1)(a)(ii) of the principal Act so that certain leases of over three years duration are excluded from the definition of "*overseas investment in sensitive land*" is supported in principle.

16. However, the duration of leases referred to in the Bill, and the principal Act is still short. For

example, a lease of more than 10 years is very common in the commercial and industrial leasing industry and is not equivalent to a freehold interest in land.

17. The Law Society has previously submitted on this point,[2] noting that the short term leases of three years are at odds with market forces and are a disincentive for applicants. It was suggested that the benchmark provided in the Resource Management Act 1991 of 35 years be used.[3]

18. It is therefore recommended that consideration be given to extending the 10 year threshold to the 35 year threshold used in the Resource Management Act.

Proposed amendments to section 16A of the principal Act – clause 8

Amendments to "Benefit to New Zealand" test

Proportionate Approach – new section 16A(1A)(b)

19. The Bill provides for the relevant Ministers to take a proportionate approach to whether the benefit to New Zealand test is met, including taking into account whether that benefit is proportionate to the sensitivity of the land and the nature of the overseas investment transactions. This has been recognised in current application assessments.[4] The approach of including this explicitly in the principal Act is supported.

Counterfactual Test– new section 16A(1A)(a)

20. The movement away from the "with v. without" test and to a counterfactual test based around the status quo is supported.

Modified Benefit Test for Farm Land – new section 16A(1C)

21. At present, the proposed economic only factors for inclusion in new section 16A(1C) are applied via the Ministers' Directive Letter to the OIO. It is suggested that this process of adjusting and refining the application of the benefits test for farm land (and other categories) should remain, as is currently the case, to retain future flexibility in light of the ever-changing economic and other policy considerations. Section 34 of the principal Act (which section is not being amended by this Bill) allows the government to alter policies on foreign investment through the Directive Letter mechanism, including those that relate to rural land.

22. The Law Society has no concerns with the continuation of requiring rural land related acquisitions to produce a "substantial" benefit to New Zealand (assuming the new proportionate approach is also applied to that). However, new section 16A(1C) interferes with the application of new section 17, in which the benefit factors are spelt out. The flexibility provided in new section 16(1E) to allow Ministers to give other factors high relative importance is useful, but it undermines the need to make special provision for rural land acquisitions as this is already accommodated in section 17.

23. Further, the use of "*high relative importance*" in the rural acquisition test raises interpretation questions over how the weightings are applied to the economic factors, and to the other factors. For example, one interpretation is that all increases in employment

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2 NZLS submission 24 May 2019 to Treasury (*Overseas Investment Act reform, phase 2 – consultation*), at p5. Submission available here: https://www.lawsociety.org.nz/__data/assets/pdf_file/0003/135147/I-Treasury-Overseas-Investment-phase-2-24-5-19.pdf.

3 Where it is deemed that leases of part of an allotment of over 35 years is a subdivision.

4 See paragraph 32.7 of the Ministerial Directive Letter dated 28 November 2017.

must always be treated as achieving high relative importance. Alternatively, it could be interpreted that if there will be only modest employment retention or increases, they will receive no weighting because they fail to achieve a high weighting. This approach also seems to preclude Ministers giving high or moderate weightings to the other non-economic benefit factors (for example, additional investment for development, environmental benefits, access and other section 17 factors), which does not seem to be a sound policy. This amendment may very well create legal uncertainty in relation to an important sensitive land category, being farms. Retaining the existing Directive Letter approach avoids the stricter application of statutory interpretation principles, which seems preferable in these situations given the wide range of possible benefits that may be raised and the judgemental nature of the consent process.

Proposed new section 17 of the principal Act – clause 9

Amendments to "factors for assessing benefit of overseas investments in sensitive land"

24. The proposed amendment combines and groups the current list of factors into broader categories such as economic, environmental, access, heritage and other factors. Further, the additional factors in the regulations will be repealed.

25. The current practice of the OIO is to require applicants to address all the existing factors in the application, even if only to say they are not claimed or are irrelevant. This proposed change would move away from this practice and leave it to the applicant to put forward what it claims are benefits, using some of the examples and perhaps other novel factors within the groupings. The less prescriptive approach is preferable, although this is in contrast with the modified benefit test for rural acquisitions which spells out the mainly economic factors that will determine whether consent will be given. There is a potential consequence that the factors set out in the modified benefit test will be what applicants focus on for all applications as offering better chances of success.

26. Clarification is sought as to whether existing section 17 factors (i.e. additional investment for development purposes, added market competition, enhanced domestic services and offering special land to the Crown) still apply, as these have not been reproduced as examples.

27. Proposed section 17(2) requires clarification. This sets out how the benefit factors must be considered. Subsection (2)(a) requires all subsection (1) factors to be considered, including parts of them. Are the “examples” given in subsection (1) “parts” of the factors? For example, will increases in productivity always be considered or only if the applicant puts it forward as a benefit?

28. Proposed section 17(2)(b) sets outs out how the new counterfactual assessments will be carried out.[5] The approach that only comparable benefits should be netted (which is the current practice) is supported, as attempting to net non-comparable factors is highly problematic and that possibility should be prevented beyond doubt.

29. The Bill does not include a requirement on Ministers to record written reasons for giving or declining consent. While the practice is to provide written reasons, there is no requirement to do so, including if consent is declined. It is suggested this is included in the Bill if it is to continue as a practice.

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[5] With the exception of water bottling situations which is given special treatment in proposed section 17(3) – this allows non-comparable negative impacts to be deducted from benefits.

Proposed new section 20 of the principal Act – clause 10

Amendments to "Exemptions from farm land offer criterion"

30. The proposed new section 20 expands on the grounds where the relevant Ministers may grant exemptions to the requirements of the principal Act where the farmland is offered on the open market to persons who are not overseas persons as set out in the regulations.[6]

31. The Bill changes advertising requirements for farm land, in particular that advertising must occur before the transaction is entered into. It is recommended that the existing advertising regime remain so that advertising could still occur after the contract is signed. There is a potential consequence that the proposed new section 16(1)(f) may have a negative impact, such as:

    31.1. discouraging investors from multiple farm land purchases (which may be of benefit to New Zealand); or

    31.2. exemptions would be obtained from the advertising requirement (meaning fewer opportunities for New Zealanders to purchase).

32. This proposed advertising requirement does not fit with common practices. Examples include:

    32.1. where transactions occur "off market"; or

    32.2. an overseas buyer who wishes to approach multiple landowners at one time (a residential developer for instance, or an investor in a significant project requiring large tracts of greenfields land for new plant/buffer zone purposes).

33. The previous practice of advertising after the fact enabled multiple transactions to reach the contract stage. If the advertising clauses were set up correctly, the applicant still faced the risk of the vendor receiving a higher offer and the contract being cancelled.

34. Instead, under the proposed reforms an overseas person will have to either:

    34.1. convince a prospective vendor to advertise their land (with attendant cost and disruption) without knowing the overseas person will buy it; or

    34.2. buy without an advertising requirement and take a risk on whether their application for an exemption will then be approved.

35. The result is that there are likely to be many more applications for exemptions to the advertising requirements.

Proposed new section 38A of the principal Act – clause 16

New section: "Information for tax purposes"

36. The detail of what will be provided to IRD is to be set out in regulations. Those regulations and that required information is not yet known. There is a concern that this may be extensive and:

    36.1. create further complexity; and

    36.2. be required for all applications (large and small and no matter how simple). As residential properties are captured there is a question as to how widely the IRD information would apply.

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6 See section 16(1)(f) in the current principal Act.

37. The Bill is not clear whether the provision of information will affect or slow down the consent process (i.e. whether IRD report to the OIO confirming it has all the information before consent will be provided). While that possibility appears to be outside the section 17 consent requirements and the purpose of new section 38A, it is recommended that section 38A should make it clear the provision of information is entirely separate from the consent regime.

Proposed new clause 2(b), Schedule 1A of the principal Act – Schedule 2 of the Bill

Definition of "a previous interest"

38. For clarity and ease of reading, it is suggested that clause 2(b) of the new Schedule 1A be amended to read "*was consecutive in time to the relevant interest in land or to another previous interest of the relevant interest in land*".

Proposed new clause 8, Schedule 5 of the principal Act – Schedule 3 of the Bill

A new Schedule 5 to be inserted in the principal Act to address fresh or seawater areas

39. This clause purports to extinguish all estates or interests in a fresh or seawater area on acquisition of that area by the Crown, except for any estate or interest specified in regulations that continues to apply.

40. There are two concerns:

    40.1. First, that while there is provision for the owner and the Crown to agree compensation payable for the fresh or seawater area itself, there is no provision for consultation with or compensation being payable to the holder of any other right that is extinguished by the Crown acquiring that area. For example, if farm land is being acquired by an overseas person subject to an existing farm lease, and the Crown acquires a fresh or seawater area contained in that farm land, the farm lease will be extinguished in respect of the fresh or seawater area without reference to the tenant. That fresh or seawater could, for example, constitute an essential accessway from one part of the farm land to the other part, the loss of which could render part of the farm land unusable.

    40.2. Secondly, the lack of clarity over what estates or interests are captured by this clause, and the proposal to set out those estates and interests in regulations. If the proposal is for the compulsory extinguishing of an estate or interest in land (particularly for holders of a registered interest), this could be a breach of that holder's rights and should be included in the Act, rather than left to regulations.

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