



Overseas Investment Amendment Bill



Why is the Overseas Investment Act being changed?

Five days after the New Zealand Labour Party and New Zealand First coalition government took office, they announced their plan to amend the Overseas Investment Act 2005.

The new government believes that overseas speculators have been artificially inflating house prices and that this is making it difficult for New Zealanders to purchase their own home.

The government is using the Overseas Investment Amendment Bill to ban overseas investors from purchasing existing residential houses and stop overseas investors from engaging in residential speculation.

This has been one of the new governments key campaign policies. It was intended to be implemented within 100 days of taking office.

Once the Overseas Investment Amendment Bill comes into effect, only New Zealand citizens, permanent residents, certain resident class visa holders, companies with over three quarters New Zealand ownership and Australian individuals will be able to buy residential property without being subject to scrutiny from the Overseas Investment Office (OIO).

What exactly are the proposed changes under this Bill? What potential knock on effects could this have on the residential development and commercial property markets?

How will the Act change?

The government is proposing to include residential land under the definition of sensitive land within the Overseas Investment Act. This will stamp out overseas speculators in the residential market.

The law in its current form excludes residential land under the definition of sensitive land. This means the majority of overseas buyers can currently purchase residential land without getting consent from the OIO.

However, under the proposed Overseas Investment Amendment Bill, residential land would be deemed sensitive.

Currently only waterfront property over a certain size, offshore islands, conservation land, land subject to a heritage order and rural land larger than five hectares, fall under the definition of sensitive land. Acquisitions that exceed \$100 million and land over a certain size that adjoin sensitive land, also fall under the current definition of sensitive land.

Under the proposed Bill, overseas purchasers will now need to satisfy one of three tests before they can purchase residential land in New Zealand.

While simple in theory, the new Bill as it stands, could have unintended consequences for the commercial property market. It will increase transaction costs and cause unnecessary delays. It is even possible that the proposed changes will make housing in New Zealand even more unaffordable. This is at the heart of what the Bill is trying to overcome.

What is the definition of residential land?

Deeming residential land as sensitive has become the most contentious issue of the proposed Bill.

The Overseas Investment Amendment Bill defines residential land as all land categorised as residential or lifestyle for rating valuation purposes under each regional territorial authorities district valuation roll.

This method of classifying residential land has the effect of casting a wide net over assets which are not necessarily residential, but are classified as such for rating purposes.





Overseas Investment Amendment Bill

This will include apartments, rental flats, lifestyle blocks and unit title car parks in residential buildings. However, the definition could also include bare development land for apartments and residential subdivisions. This will force overseas purchasers to apply for Overseas Investment Office consent.

The Bill also makes no distinction for an overseas purchaser buying residential land for non-residential purposes (for example residential land to be used for the development of a hotel). The development of long term accommodation facilities such as retirement villages, rest homes and university accommodation could also be caught under the definition of residential land.

A high profile example of these unintended consequences of the Bill involves Spark, one of New Zealand's largest telecommunication companies. Interestingly, because Spark is predominantly owned by offshore interests, it will need to obtain Overseas Investment Office consent when they build any new cell towers on residential land.

The effect of adding residential and lifestyle land to this new classification means that the number of OIO applications will skyrocket from around 100 cases per annum to potentially thousands. The New Zealand Treasury estimates it could affect 4,700 transactions per year.

This will significantly raise transaction costs and delay the settlement period for residential land purchased by overseas interests. But will foreign investors even bother with the new rules? Will they invest in alternative countries that offer more straightforward legislation?

Will the new Bill create an uneven playing field for companies which are run and headquartered in New Zealand but have registered overseas shareholders? Interestingly, a company whose securities are held by overseas incorporated custodians or nominees would come under the

definition of offshore ownership, even if 75% of those securities are held by New Zealand citizens.

If the Bill passes in its current form, given the additional compliance costs, the length of time involved to achieve consent, and the settlement risk this places on vendors, will it result in an anti-competitive business environment with an uneven playing ground for offshore companies?

What tests do foreign purchasers need to pass?

Under the proposed Bill, overseas investors buying residential land will be required to satisfy certain character tests. In order to obtain consent from the OIO, one of three tests need to be passed:

1. The commitment to New Zealand test:

An overseas buyer can buy residential land under the proposed Bill if they can demonstrate a commitment to residing in New Zealand. If the overseas person is a New Zealand citizen, a permanent resident or is the holder of a residence class visa, they can pass this test. Consent is conditional on the overseas investor occupying the property as their main home or divesting the asset within 12 months of the investment, should the investor fail to meet their requirements under the commitment to New Zealand test.

Market commentators fear this test will discourage high-net-worth investors from buying further properties in New Zealand. These individuals contribute significantly to the New Zealand economy. If overseas buyers do not meet this test they will have to satisfy one of the other two tests which are potentially far more cost prohibitive.





Overseas Investment Amendment Bill

Construction companies are concerned that the new requirement for OIO consent on residential homes will reduce the demand from wealthy offshore individuals for high value homes.

2. The benefit to New Zealand test:

An overseas buyer can purchase residential land under the proposed Bill if they can demonstrate the way in which the land could be developed will have wider benefits to New Zealand. However, in order to use this entry path, the applicant must either:

- a. increase the supply of housing on the land,
- b. dispose of the residential land after a specified period, or
- c. not use the land for residential purposes, such as the development of a hotel, a supermarket, or a shopping complex.

3. The increased housing on residential land test:

An overseas buyer can buy residential land under the proposed Bill when they develop the land in a way that increases housing supply in New Zealand. Consent will be conditional on the overseas investor developing the land and onselling dwellings within a specified period, or constructing and extending the operation of a long term accommodation facility. Undertaking development works to support the development of housing, such as the subdivision of a site and onsale of sections, will also be allowed. One drawback of this test is that if a purchaser is buying an existing long term accommodation facility which is incapable of being expanded then the purchaser will have to apply under the benefit to New Zealand test.

Because of the requirement to sell new dwellings within a defined period, which is typically 12 months, developers are concerned about the possibility of being forced to sell finished houses in a declining market.

Many developments are also subject to presale requirements in order to achieve bank funding. If overseas investors are not permitted to purchase residential units as long term investments, developments may not achieve their required presales and some projects might not proceed. This will have the unintended consequence of reducing the overall rental pool in New Zealand and will ultimately raise rental rates. Auckland's apartment market would be severely impacted by this Bill. If it were not for offshore investors, thousands of apartments in Auckland would never have been built.

Would it not be better to adopt the Australian model? This allows offshore buyers to purchase new dwellings and keep them indefinitely, provided they either live in the dwelling or rent it out. This would have the effect of increasing the total pool of housing in New Zealand.

What positive changes have been introduced under the Bill?

One bright spot within the new Bill is the introduction of standing consents. Standing consents will essentially give overseas investors pre-approval to buy residential land. Investors purchasing residential land, that can demonstrate they are meeting the criteria under the commitment to New Zealand test or the increased housing test, will now be able to apply for a standing consent. Once the consent has been granted the holder will be required to keep the OIO informed that they are meeting the pre-approved conditions under their consent for each transaction.

Purchasers lodging for OIO approval under the benefit to New Zealand test, such as developers of hotels, supermarkets and shopping complexes, typically purchase land that can sometimes be classed as residential to





Overseas Investment Amendment Bill

meet their objectives. However, under the proposed Bill, standing consents will only apply to those purchasing residential land under the commitment test or the increase in housing test. These parties will be required to apply for OIO consent for each transaction.

Where to from here?

The Government is fast-tracking the Overseas Investment Amendment Bill to make sure that any changes are in place before the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (the TPP Agreement successor) enters into force. Market commentators have highlighted a number of problems and potential loopholes with the amendment Bill. They predict the act may inadvertently restrict the supply of residential housing, cause significant time delays and increase the cost of doing business in New Zealand.

To meet the government's goal of increasing the housing supply by 100,000 homes in the next ten years, significant investment will be required. However, there is a limited pool of New Zealand based developers who can deliver housing on this scale. Will the proposed rules discourage overseas developers from entering our market? Furthermore, if foreign individuals are deterred from buying homes and apartments, will the new rules precipitate a collapse in the apartment market with investors being banned? Will this reduce the available housing supply to the rental market and subsequently force rents up?

Although this process is being rapidly pushed through, a regulatory impact statement prepared by the New Zealand Treasury, states that the aim of the Government's policy is not to impede the broader objective of increasing the supply of residential housing.

Timeline

The select committee is currently reviewing public submissions. A report on their findings and suggestions for changes is due to be made available on 31st May, 2018. The earliest date the second reading of the Bill can commence is on the 14th of June. If the second version of the Bill passes, parliament will debate the Bill. Following on from that, a third and final reading of the Bill will take place and can be voted on.

If the Overseas Investment Amendment Bill passes, it will become an Act ten days after it receives Royal assent from the Governor-General. Given there was unanimous support from Labour, New Zealand First and the Green party during the first reading, based on a fast tracked timeline, the Overseas Investment Amendment Bill is likely to come into force in July or August of 2018.

Is this timing too premature given that the Overseas Investment Amendment Bill's unintended consequences have not been fully explored and debated?

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