

# Regulation of foreign investment in residential property

## Overview

- 2.1 Australia's regulatory framework for foreign investment in residential real estate is intended to increase Australia's housing stock. Consistent with this aim, the rules that apply to a non-resident investor in an Australian dwelling are based on whether the investment will produce such an increase.<sup>1</sup>
- 2.2 Foreign investment applications are considered in light of this overarching principle and in the case of new dwellings are usually approved without conditions. Foreign nationals are prohibited from buying established homes but temporary residents can apply to purchase one established dwelling to use as a residence while they live in Australia.<sup>2</sup>

## The law

- 2.3 The *Foreign Acquisitions and Takeovers Act 1975* (the Act), the *Foreign Takeovers (Notices) Regulations 1975* and the *Foreign Acquisitions and Takeovers Regulations 1989* comprise the legislation governing foreign investment in Australia.
- 2.4 The Act governs the acquisition of Australian urban land (which includes residential real estate) by foreign persons.<sup>3</sup> Specifically, section 12A of the Act applies to acquisitions, or proposed acquisitions, of interests in

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1 The Treasury, *Submission 31*, p. 1.

2 The Treasury, *Submission 31*, p. 1.

3 The Treasury, *Submission 31*, p. 2.

'Australian urban land'.<sup>4</sup> A foreign person is defined as a person who is neither an Australian or New Zealand citizen nor a permanent resident of Australia.<sup>5</sup>

- 2.5 Section 26A of the Act requires a foreign person to notify the Treasurer of a proposal to acquire or increase an interest in Australian urban land, unless the acquisition is exempt under the regulations. Formal notification of a proposal under section 26A must be made in accordance with the forms prescribed in the *Foreign Acquisitions and Takeovers (Notices) Regulations 1975*.<sup>6</sup>
- 2.6 Section 21A of the Act outlines the powers available to the Treasurer in relation to foreign investment proposals to acquire interests in Australian urban land. The Act does not provide the Treasurer with the power to approve investment proposals but to prohibit any proposals that are deemed contrary to the national interest.<sup>7</sup> Additionally, the Treasurer may order the divestment or unwinding of investment where acquisitions are found to have been contrary to the national interest.<sup>8</sup>
- 2.7 Section 25 of the Act allows conditions to be applied to the approval of an investment proposal that are necessary to remove national interest concerns that would otherwise arise.<sup>9</sup>

## The Foreign Investment Review Board

- 2.8 The Foreign Investment Review Board (FIRB) is a non-statutory body established in 1976 to advise the Treasurer and the Government on Australia's Foreign Investment Policy (the Policy) and its administration. FIRB's functions are advisory only. Responsibility for making decisions on the Policy and proposals rests with the Treasurer. The Treasury's Foreign Investment and Trade Policy Division provides secretariat services to FIRB and is responsible for the day to day administration of the arrangements.<sup>10</sup>
- 2.9 The role of FIRB, including through its secretariat, is to:
- examine proposed investments in Australia that are subject to the Policy, the Act, and supporting legislation and to make

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4 Foreign Investment Review Board (FIRB), *Annual Report 2012-13*, p. 65.

5 FIRB, *Annual Report 2012-13*, p. 48.

6 FIRB, *Annual Report 2012-13*, p. 64.

7 FIRB, *Annual Report 2012-13*, p. 65.

8 FIRB, *Annual Report 2012-13*, p. 66.

9 FIRB, *Annual Report 2012-13*, p. 66.

10 FIRB web site <<http://www.firb.gov.au/content/who.asp?NavID=48>>viewed 15 September 2014.

recommendations to the Treasurer and other Treasury portfolio ministers on these proposals;

- advise the Treasurer on the operation of the Policy and the Act;
- foster an awareness and understanding, both in Australia and abroad, of the Policy and the Act;
- provide guidance to foreign persons and their representatives or agents on the Policy and the Act;
- monitor and ensure compliance with the Policy and the Act; and
- provide advice to the Treasurer on the Policy and related matters.<sup>11</sup>

## Current regulations

- 2.10 All foreign investment in Australian real estate is screened by the Treasury through a prior approval process as outlined below.
- 2.11 Australia's Foreign Investment Policy sets out the rules against which the activities of foreign investors in Australian residential real estate are generally assessed. Different rules apply depending on whether the property being acquired will increase the housing stock or is an established dwelling.<sup>12</sup>
- 2.12 All foreign persons can apply to purchase vacant residential land for development and new dwellings in Australia. Applications to purchase vacant land are generally approved on the condition that construction begins within 24 months.<sup>13</sup> The completed dwellings may then be rented out, sold or retained for the foreign investor's own use. Applications to purchase new dwellings are usually approved without conditions.<sup>14</sup>
- 2.13 Additionally, all foreign persons can seek approval to redevelop an established dwelling. These applications are normally only approved where the redevelopment results in a net increase in available housing or in instances where the existing dwelling is found to be derelict or uninhabitable.<sup>15</sup>
- 2.14 The purchase of established dwellings in Australia by foreign persons is generally restricted to temporary residents.<sup>16</sup> The current policy states that temporary residents may purchase one established dwelling to be used as

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11 FIRB <<http://www.firb.gov.au/content/who.asp?NavID=48>>viewed 15 September 2014.

12 The Treasury, *Submission 31*, pp. 2-3.

13 FIRB <[http://www.firb.gov.au/content/\\_downloads/AFIP\\_2013.pdf](http://www.firb.gov.au/content/_downloads/AFIP_2013.pdf)>viewed 20 November 2014

14 The Treasury, *Submission 31*, p. 3.

15 The Treasury, *Submission 31*, p. 3.

16 The Treasury, *Submission 31*, p. 3.

their residence in Australia but must sell this property when it ceases to be their residence.<sup>17</sup> The standard practice at the Treasury is to allow three months for this sale to occur.<sup>18</sup>

**Fact Box****Q: Can a foreign person buy residential real estate in Australia?**

A: Yes, but there are restrictions for existing homes. A non-resident foreign investor is generally prohibited from purchasing an existing home. A temporary resident (who has a visa of more than 12 months) can purchase one existing home to live in for the duration of their visa but must sell within three months of leaving Australia at the expiration of their visa.

**Q: What types of residential real estate can be bought by a foreign investor?**

A: All foreign investors can purchase new dwellings but all purchases must be approved – in advance of purchase – by FIRB. This policy is intended to attract investment in new housing development to increase Australia's housing stock.

**Q: Can a foreign person purchase residential real estate with an Australian citizen?**

A: If the foreign person is married to an Australian citizen, the answer is yes. Otherwise, all of the standard rules apply as if the foreign person was purchasing the residential real estate in their name only (see answers to earlier questions).

**Q: Can a permanent resident purchase residential real estate?**

A: Yes. There are no restrictions on permanent residents, just as there are no restrictions on Australian citizens.

- 2.15 Property developers can apply for an advanced-off-the-plan certificate to sell all new properties in a development of 100 or more dwellings to foreign persons, provided the development is also marketed locally.<sup>19</sup> An individual foreign buyer is not then required to gain separate approval to purchase dwellings in a certified development.<sup>20</sup> Currently, no penalties

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17 FIRB <[http://www.firb.gov.au/content/\\_downloads/AFIP\\_2013.pdf](http://www.firb.gov.au/content/_downloads/AFIP_2013.pdf)>viewed 18 July 2014.

18 FIRB <<http://www.firb.gov.au/content/faq.asp#temporary>>viewed 13 November 2014.

19 The Treasury, *Submission 31*, p. 4. See also Table 2.1.

20 The Treasury, *Submission 31*, p. 4.

exist for breaches of this provision of the Act other than the cancellation of a certificate.<sup>21</sup>

- 2.16 Changes have been made to the regulatory framework for foreign investment in residential real estate over several decades. The key changes to this framework are highlighted in Table 2.1.

## Administration of the policy

- 2.17 All foreign nationals must seek approval before acquiring interest in Australian real estate, unless the acquisition is exempt. The Treasury's Foreign Investment and Trade Policy Division is responsible for the day-to-day administration of Australia's real estate screening arrangements, in consultation with FIRB.<sup>22</sup> As noted earlier, FIRB's functions are advisory and the responsibility for making decisions on the Policy and proposals rests with the Treasurer.<sup>23</sup>
- 2.18 The Treasurer has provided an authorisation to the Executive Member of FIRB, who manages the Foreign Investment and Trade Policy Division, and other senior Division Staff, to make decisions on proposals that are consistent with the Policy which do not involve issues of special sensitivity. In 2012-13, such proposals comprised over 93 per cent of all foreign investment proposals decided and were mostly real estate purchases.<sup>24</sup>

### Fact Box

- The Treasury's Foreign Investment and Trade Policy Division is responsible for the day-to-day administration of Australia's real estate screening arrangements, in consultation with FIRB. This Division employs around 30 staff and 8 of these staff are dedicated to residential real estate.
- The FIRB itself comprises five part-time members, including a Chairman, and one full time Executive member from the Foreign Investment and Trade Policy Division. The FIRB members have expertise in business, taxation, superannuation, banking, corporate finance, fund management, and agriculture.

21 Mr John Hill, Manager, Compliance and Real Estate Screening Unit, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 13.

22 The Treasury, *Submission 31*, p. 11.

23 FIRB, *Annual Report 2012-13*, p. 3.

24 FIRB, *Annual Report 2012-13*, p. 6.

- 2.19 Proposals involving transactions that are not covered by this delegation are referred to Treasury Ministers for a decision. These arrangements streamline the approval process and facilitate decisions on applications within statutory deadlines.<sup>25</sup>
- 2.20 The application process requires information about the relevant parties and their proposals to be submitted online. Information sought from applicants varies according to the property investment category, the residency status of the investor and whether an investor is an individual or corporation.<sup>26</sup> Approvals are considered on a case-by-case basis and foreign persons must submit proposals that identify specific property for assessment.
- 2.21 More screening emphasis is placed on applications from temporary residents to purchase established residential property. These applicants are required to affirm their residency status and declare their property usage intentions.<sup>27</sup> In examining proposals, the applicant's compliance with any conditions relating to past proposals is taken into consideration. Instances of failure to comply with conditions may result in future proposals being rejected.<sup>28</sup>
- 2.22 Property developers of a proposed new residential project can apply for advanced-off-the-plan certificates for a development of 100 or more dwellings. The developer is permitted to sell all of the dwellings to foreign buyers but must also market the properties in Australia. The conditions of these certificates require the developer to report details of all foreign persons that have acquired a dwelling in the development.<sup>29</sup>
- 2.23 If an off-the-plan dwelling with such a certificate is then on-sold by a foreign owner, it is no longer considered a new property and is therefore subject to the restrictions on foreign purchases of established properties as outlined later in this chapter.
- 2.24 Applications that are not consistent with the foreign investment policy are not approved. In this situation, applicants often withdraw their application before a final order prohibiting the transaction is issued.<sup>30</sup>

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25 The Treasury, *Submission 31*, p. 11.

26 The Treasury, *Submission 31*, p. 11.

27 The Treasury, *Submission 31*, p. 12.

28 FIRB, *Annual Report 2012-13*, p. 10.

29 The Treasury, *Submission 31*, p. 4.

30 The Treasury, *Submission 31*, p. 12.

**Fact Box**

**Q: Can a non-resident foreign investor buy a newly built house or apartment that has previously been owned by a non-resident foreign investor?**

A: No, all properties purchased by non-resident foreign investors must be brand new.

**Q: Can a foreign person who has been granted a temporary residency visa seek approval and buy an established property as a primary residence before arriving in Australia?**

A: No, a temporary resident must be in Australia in order to seek approval to purchase an established property as a home. A temporary resident can buy a single established dwelling to live in if they have a visa that permits them to be legally resident in Australia for a continuous period of more than 12 months.

**Q: Are there any circumstances in which a non-resident foreign investor can purchase an existing home?**

Yes, in very specific circumstances - that is, an established dwelling can also be purchased by a foreign investor if it is to be redeveloped and replaced with at least two new residences or if a derelict residence is to be redeveloped to become habitable. Otherwise, a non-resident foreign investor is prohibited from purchasing an existing home.

Table 2.1 Changes to the Foreign Investment Framework for Residential Real Estate

Year	Change
1976	Under the Government's Foreign Investment Policy (at the time the primary mechanism under which real estate investment was screened), some acquisitions of Australian real estate by foreign interests were examinable. However, acquisitions of residential dwellings for the intended use by expatriate Australians and accepted migrants and transfers of real estate between immediate family members were not examinable. The Foreign Investment Review Board was established.
1978	All acquisitions of real estate by a single foreign interest or associated foreign interests up to a cumulative value of less than \$250,000 (since 8 June 1978) did not require approval. Proposals from foreign developers to construct and sell real estate developments (including exclusively to Australians) were subject to a minimum 50 per cent Australian equity participation.
1981	All acquisitions of real estate by a single foreign interest or associated foreign interests up to a cumulative value of less than \$350,000 (since 8 June 1978) did not require approval.
1985	All acquisitions of real estate by a single foreign interest or associated foreign interests up to an aggregate value of less than \$600,000 (since 8 June 1978) did not require approval. Requirement of 50 per cent Australian equity participation removed for developments that are minor (less than \$10 million) or short-term in nature (less than five years to complete).
1987	\$600,000 threshold was abolished, with all proposed acquisitions of urban (including residential) real estate by foreign interests requiring approval regardless of size or value. Advanced-off-the-plan category was introduced with a minimum requirement of four or more dwellings in a development provided that no more 50 per cent of the units in any one project were bought by non-residents and subject to an undertaking by the developer to report all sales six monthly so that compliance with the 50 per cent restriction could be monitored.
1989	<i>Foreign Takeovers Act 1975</i> renamed <i>Foreign Acquisitions and Takeovers Act 1975</i> . Statutory backing given to the Government's Foreign Investment Policy, with existing restrictions requiring foreign persons to seek approval for the purchase of Australian urban real estate replicated in the Act.
1999	Advanced-off-the-plan certificates: only developers seeking advanced approval to sell up to 50 per cent of a development with ten or more (previously four or more) dwellings to foreign investors could apply for advanced approval.
2008	The requirement for temporary residents to obtain foreign investment approval for real estate purchases was removed. The 50 per cent rule for the advanced-off-the-plan category was removed and replaced with a new requirement that the developer must market the development domestically and the minimum number of dwellings required in a development was increased to 100.
2010	The requirement that temporary residents need approval for real estate purchases was reinstated.

Source *The Treasury, Submission 31, Attachment A, p. 14.*

2.25 The Act provides a 30-day statutory examination period for a decision to be made on proposals lodged under the Act, followed by a further 10 days to notify the applicant of the decision.<sup>31</sup> If the Treasurer does not take action within this period, the power to prohibit the proposal or impose

31 FIRB, *Annual Report 2012-13*, p. 6.

conditions expires.<sup>32</sup> The 30-day examination period may be extended by up to a further 90 days by the issue of an Interim Order which prohibits the proposal for that period.<sup>33</sup> Interim Orders are generally issued to allow the applicant additional time to provide adequate information for assessing the proposal.<sup>34</sup>

- 2.26 FIRB publishes data annually on its activities, including the total number and value of the approvals it grants to foreign investors and temporary residents for the purchase of a specifically identified property or piece of land.<sup>35</sup> However, FIRB does not record actual purchases.
- 2.27 FIRB cautions that there are substantial differences between statistics on proposed investments and actual investment flows.<sup>36</sup> Approvals data do not correspond with the number of actual purchases by foreign investors as not all approvals will result in a sale to the applicant. For example, investors may seek several approvals to allow them to bid at different auctions but may only purchase one property or none at all.<sup>37</sup>
- 2.28 Advanced-off-the-plan certificates are recorded as one approval regardless of the number of dwellings sold to foreign persons, and the value of the advanced-off-the-plan approvals is recorded as the total value of the development, even though not all of the dwellings may end up being sold to foreign purchasers.<sup>38</sup>

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32 FIRB, *Annual Report 2012-13*, p. 64.

33 FIRB, *Annual Report 2012-13*, pp. 64-65.

34 FIRB, *Annual Report 2012-13*, p. 6.

35 Reserve Bank of Australia (RBA), *Submission 19*, p. 2.

36 FIRB, *Annual Report 2012-13*, p. 15.

37 The Treasury, *Submission 31*, p. 6.

38 The Treasury, *Submission 31*, p. 6.

**Fact Box**

**Q: Can a foreign person in Australia on a 12 month tourist visa buy an established property to live in?**

A: No. This does not satisfy the temporary residency requirements for purchasing an established property as a primary residence.

**Q: Can non-residents jointly acquire an established property with a legally resident family member?**

A: Non-residents cannot acquire an interest in an established residential property unless it will result in an increase in Australia's housing stock or it is a joint purchase with a spouse who is an Australian citizen or permanent resident.

**Q: Can non-resident parents buy an established property for a child who is legally resident in Australia?**

A: A non-resident cannot purchase an established property in their name in order to provide a home for a legally resident child. However, if an established property was purchased in the name of a temporary resident child as a primary residence, this would be lawful.

- 2.29 The committee notes from the evidence received by this inquiry that there are three significant limitations to the current data on foreign investment in Australian property. Foreign buyers of residential real estate who fail to apply for pre-approval are not captured by the data and are therefore an unknown quantity. In addition, the data that is captured is not always accurate as not all approvals result in a purchase. Finally, there are problems with the timeliness of the data – given the considerable delay in data release by FIRB. Issues regarding FIRB data are discussed in more detail in Chapter 3.

**Fact Box**

**Q: Can a previous temporary resident who has left Australia continue to own a new apartment that was their former home in Australia?**

A: Yes, if this apartment was brand new when it was purchased, then it can be retained by the former temporary resident as all brand new dwellings can lawfully be purchased and retained by foreign investors regardless of their residency status.

**Q: Can a previous temporary resident who has left Australia continue to own an established apartment or house that was their former home in Australia?**

A: No, an established property purchased by a previous temporary resident as a home whilst in Australia cannot be retained if it ceases to be their primary home. Such properties must be sold within three months of the foreign owner no longer living there. They cannot be retained by a non-resident as an investment property or as a second home. This restriction would also apply to any temporary resident who decided to move house whilst in Australia.

**Q: Can a temporary resident buy additional properties or real estate whilst in Australia?**

A: Only if they are brand new houses or apartments, or vacant land for residential development. A temporary resident cannot buy an established property unless it is to be used as a primary residence. An established property cannot be bought by any foreign investor, including temporary residents, as a second home, holiday home or as an investment.

## Approval process

2.30 The Treasury operates an online system to process applications from foreign nationals for approval to purchase land and property. Mr John Hill, Manager, Compliance and Real Estate Screening Unit at the Treasury broadly outlined aspects of this process at the public hearing on 30 May 2014 in Canberra:

We scan centrally as database line items the applications that flow from the website portal into our case management system. It is a more streamlined process for new and vacant land. In a sense we triage the volumes of cases that arrive each morning. Basically we pick out anything that looks particularly interesting for compliance or anomaly. We look at whether there are collective owners of applications. They may be entities, trusts, companies et cetera. They are perfectly able to acquire under the policy new and

vacant land. The important thing is that people are well identified and that we make sure there are no gaps in the information.<sup>39</sup>

- 2.31 Mr Hill commented further that these online forms are now the primary mechanism by which these applications are received and that they take 10 to 15 minutes to complete. He advised:

When they submit that form, their details are transferred through the internet to the Treasury management system. Typically we will get a range of diagnostic information from the applicant, and the process of screening commences at that point.<sup>40</sup>

- 2.32 Mr Hill also outlined the types of screening that occur when approval applications for new properties are submitted. He stated:

I would estimate that about 10 per cent of all new and vacant land applications that we get each day would probably be slightly peculiar – not necessarily a problem but they would trigger a review process. If the value of the transaction is beyond a certain threshold, we immediately consult with law enforcement agencies. We will look at names and incorrect completion of declaration forms. People need to clearly accept the terms and conditions of the property acquisition. If that has not been done, we will ping it. The 10 per cent goes off to a team of staff that looks very closely at those applications and in most cases will probably contact the applicant to clarify. The rest of them are summarily approved, and that can take in the order of 24 hours from receipt.<sup>41</sup>

**Fact Box**

**Q: Can foreign investors purchase vacant land to build new housing?**

A: Yes, but the granting of approval to a foreign investor to purchase vacant land for this purpose would be on the condition that construction must commence within two years. Failure to comply with this condition could result in an order being issued to the foreign owner to sell the land.

## Compliance and enforcement

- 2.33 The Treasury provided evidence that it uses a compliance framework that emphasises “information and education initiatives”, supported where

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39 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 3.

40 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 3.

41 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 3.

- necessary by more active measures to encourage foreign investor compliance.<sup>42</sup>
- 2.34 Measures the Treasury implements to manage compliance include maintaining a hotline to initiate follow-up investigations based on information provided and monitoring relevant properties to ensure conditions imposed on approved purchases are being adhered to.<sup>43</sup> The committee was not provided with any precise data in relation to the operation of this hotline. In the committee's view, detailed information on compliance activities that occur through this facility must be accurately maintained as part of future enhancements to the internal processes at the Treasury's Foreign Investment and Trade Policy Division.
- 2.35 The Act provides a range of powers to enforce decisions made, including the ability to:
- order the sale of a property purchased without prior foreign investment approval, where that purchase is considered contrary to the national interest;
  - prosecute a foreign person who failed to obtain prior approval for a purchase;
  - prosecute a foreign person who failed to comply with an order to sell shares, assets or property; and
  - prosecute a foreign person who failed to comply with conditions attached to an approval.<sup>44</sup>
- 2.36 Parties that do not comply with the conditions applied to investment proposals approved by the Treasurer commit an offence under subsection 25(1C) of the Act.<sup>45</sup>
- 2.37 On conviction for a breach of the Act individuals may be fined a maximum penalty of 500 penalty units (currently \$85,000), imprisonment for two years, or both. In the case of a corporation, a multiplier of five applies to the maximum fine for an individual, resulting in a current maximum of \$425,000.<sup>46</sup>
- 2.38 While the Act provides wide-ranging powers to enforce decisions made, Treasury provided evidence that the use of formal prohibition or divestment orders is avoided where investors cooperate with compliance staff. The Treasury works with applicants to resolve most concerns

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42 The Treasury, *Submission 31*, p. 12.

43 The Treasury, *Submission 31*, p. 13.

44 The Treasury, *Submission 31*, p. 4.

45 FIRB, *Annual Report 2012-13*, p. 67.

46 The Treasury, *Submission 31*, pp. 4-5.

relating to compliance with conditions and the experience is that there is rarely a need to resort to these penalties as most investors comply with the requirements in the Act and follow directions from Treasury staff.<sup>47</sup>

**Fact Box**

**Q: Where do the regulations on foreign investment in Australian residential real estate come from?**

A: The *Foreign Acquisitions and Takeovers Act 1975* gives the Federal Treasurer the power to block certain foreign investments that are deemed by this legislation to be contrary to the national interest.

**Q: How are these regulations enforced in relation to residential property?**

A: All foreign purchases of residential property require pre-approval from the Treasury through its Foreign Investment and Trade Policy Division which receives policy advice from the Foreign Investment Review Board (FIRB). Applications for approval are made using an online system.

**Q: What happens if the regulations are breached?**

A: There are a number of measures that can be taken for breaches of the rules. If a foreign person has unlawfully purchased or retained a property, or has failed to gain the required approval, the legislation allows the Treasurer to issue a final order which would block the acquisition of the property, or a divestment order which would require the foreign investor to dispose of the property.

- 2.39 However, the committee notes that an illegal purchase cannot be rectified without divestment. For example, a foreign buyer must not be allowed to retain an established property as an investment, when they should only be allowed to buy a brand new dwelling for this purpose. FIRB and the Treasury must ensure that there is no such circumvention of the rules and no retrospective approvals for illegal purchases. Retrospective approvals may be appropriate where a non-resident foreign investor has purchased a new dwelling but did not notify FIRB. However, sanctions may apply.
- 2.40 The Treasury has access to data sources such as the Department of Immigration and Border Protection (DIBP) online visa record system, fee-based property ownership searches and statistical databases provided under licence by external agencies to support its compliance activities.<sup>48</sup> However, the committee is aware that the most up-to-date information

47 The Treasury, *Submission 31*, p. 13.

48 The Treasury, *Submission 31*, p. 13.

from DIBP regarding the departure of temporary residents from Australia is not available to FIRB under current migration legislation. This is further discussed in Chapter 3.

- 2.41 FIRB is also responsible for monitoring compliance, and to this aim works with relevant members of the business community, government authorities, legal community and other government agencies (such as the Australian Federal Police, Department of Immigration and Border Protection, Australian Tax Office and Australian Securities and Investments Commission).<sup>49</sup>

#### **Fact Box**

**Q: Can breaches of the regulations governing foreign investment in residential real estate be subject to court prosecutions?**

A: Yes. Failure to comply with a final or divestment order from the Treasurer can result in a court proceeding to enforce these orders and can result in a fine of up to \$85,000 for an individual (or up to \$425,000 for a company), imprisonment for a maximum of two years, or both.

**Q: What penalties apply to a third party, such as a real estate agent, who knowingly assists a non-resident foreign investor to breach the rules?**

A: None. Currently, penalties only apply to the foreign investor.

## **Significant Investor Visas**

- 2.42 A mechanism exists for foreign investment in residential real estate through the recently introduced Significant Investor Visa (SIV) scheme that is operated by the Department of Immigration and Border Protection (DIBP). This scheme commenced on 24 November 2012.<sup>50</sup>
- 2.43 The SIV is intended to target the migration of high net-worth individuals to Australia with the longer-term aim of moving the wealth of international businesses so that they become Australian businesses. Investment migrants under this scheme are required to invest at least \$5 million into complying investments in Australia for a minimum of four years before becoming eligible for a permanent visa. DIBP states in its submission to this inquiry that:

Direct investment in residential property is excluded from investments that can be considered a complying investment for the purposes of the SIV. However, it is recognised that real property in

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49 RBA, *Submission 19*, p. 2.

50 Department of Immigration and Border Protection (DIBP), *Submission 50*, p. 3.

Australia is one of a range of investments that can be made by a managed fund, which may be considered a complying investment.<sup>51</sup>

**Fact Box**

Since the commencement of the Significant Investor Visa program in November 2012, a total of 286 visas have been granted up until the end of June 2014. Immigration Department data indicates that among current SIV holders, at least 7 investments worth \$27.5 million have been made into managed funds that invest in property.

- 2.44 At the public hearing in Canberra on 29 August 2014, the committee queried witnesses from DIBP on how the SIV scheme could apply to foreign investment in residential real estate. Mr Garry Fleming, First Assistant Secretary, DIBP responded:

The main comment I would make in relation to residential real estate is that it is not a qualifying complying investment for an individual to go in and buy residential real estate. Even if they are doing their investment via a private proprietary company, there is a requirement that it not be a passive investment. Therefore, for example, buying an established property for residential or rental purposes would not qualify, but potentially developing new real estate might. Otherwise, the investment is via a managed fund and there is obviously different ways that managed funds operate. Yes, the key point would be that the complying investment cannot be an individual buying residential real estate for living or rental purposes.<sup>52</sup>

- 2.45 DIBP confirmed that the holder of an SIV would be eligible to purchase an established property to live in as a temporary resident with Treasury approval but reiterated that this was entirely separate from SIV compliance requirements. DIBP emphasises in its submission that an investment into a residential property development could only qualify as a complying investment under the SIV scheme under certain conditions:

If the company operates a property development business of sizeable scale and on a consistent basis, then an investment into the company may be SIV compliant. Assessment of a qualifying

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51 DIBP, *Submission 50*, p. 3.

52 Mr Garry Fleming, First Assistant Secretary, DIBP, *Committee Hansard*, Canberra, 29 August 2014, p. 1.

business can only be on a case-by-case basis in conjunction with a valid visa application as each applicant's investment structure is different.<sup>53</sup>

- 2.46 The committee understands that Austrade will be responsible for determining complying investment policy under the SIV scheme from July 2015. It is the committee's view that the complying investment policy under the SIV program should be continually reviewed to ensure that the program is delivering investment that is in the national interest.

## International comparisons

### Overview

- 2.47 In its submission to this inquiry, the Treasury notes that individual country restrictions on foreign investment in residential real estate are difficult to compare, due in part to a lack of reliable information on such policies in many jurisdictions.<sup>54</sup>
- 2.48 The Treasury also submits that based on the available information, the United States, Canada, New Zealand, the United Kingdom and many European countries do not have explicit foreign investment restrictions or do not apply differential tax rates on foreign purchases of housing. In comparison, China, Vietnam, Singapore, Philippines, India and Thailand appear to limit foreign purchases of residential properties, and Singapore and Hong Kong impose additional stamp duties on these transactions.<sup>55</sup>
- 2.49 As the RBA commented, in China, India and Indonesia, non-residents are generally not permitted to purchase residential property.<sup>56</sup>
- 2.50 In its submission to the inquiry, SMATS Group comments that international markets are significantly more speculative than that in Australia.<sup>57</sup> SMATS Group also states that foreign investor activity in overseas real estate markets can be above half of all market activity at times (far greater than the corresponding activity in Australia), and unlike Australia, do not have a dependence on foreign investment to support the supply of housing stock.<sup>58</sup>

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53 DIBP, *Submission 50*, p. 12.

54 The Treasury, *Submission 31*, p. 5.

55 The Treasury, *Submission 31*, p. 5.

56 RBA, *Submission 19*, p. 8.

57 SMATS Group, *Submission 35*, p. 10.

58 SMATS Group, *Submission 35*, p. 10.

- 2.51 The Reserve Bank of Australia (RBA) notes in its submission with regard to industry reports that most English speaking countries have very few restrictions on foreign purchases of residential property. The RBA states that these countries make little to no differentiation between foreign purchases of new or established dwellings, and have very few reporting requirements.<sup>59</sup>
- 2.52 The RBA further comments in its submission that European governments have recently been looking to increase foreign residential investment from outside the European Union.<sup>60</sup> The RBA also notes that Hong Kong, Malaysia and Singapore have comparatively minimal restrictions on foreign investment in their new and established housing markets although some Asian countries have increased property taxes in an effort to slow the pace of house price growth.<sup>61</sup>
- 2.53 The RBA submits that Australia is among the more open countries with respect to foreign purchases of new housing.<sup>62</sup> The Property Council of Australia suggests in its submission however that Australia ranks second to Switzerland in foreign investment strictures.<sup>63</sup>

## Screening

- 2.54 At the public hearing on 30 May 2014, Mr Brian Wilson, Chairman of FIRB, commented that 'I think it is pretty clear that, amongst the OECD countries, very few countries have any particular restrictions'.<sup>64</sup> Mr Wilson stated:
- Switzerland is probably the only one of the so-called developed nations that has restrictions comparable to those of Australia... Australia is almost alone amongst the OECD countries for having actual restrictions or vetting.<sup>65</sup>
- 2.55 The Property Council of Australia submission compares 12 countries in respect of their foreign investment regulations. Of these, the countries that require approval for foreign investment in real estate are Switzerland, Australia, Singapore, Canada, and Denmark (if considered a non-

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59 RBA, *Submission 19*, p. 8.

60 RBA, *Submission 19*, p. 8.

61 RBA, *Submission 19*, p. 8.

62 RBA, *Submission 19*, p. 1.

63 Property Council of Australia, *Submission 25*, pp. 3-4.

64 Mr Brian Wilson, Chairman, FIRB, *Committee Hansard*, Canberra, 30 May 2014, p. 1.

65 Mr Wilson, FIRB, *Committee Hansard*, Canberra, 30 May 2014, p. 1.

- resident). Singapore and Australia have specific bodies that process these approvals (the Singapore Land Authority and FIRB, respectively).<sup>66</sup>
- 2.56 The countries in this comparison that do not require approval for foreign investment are Hong Kong, Japan, Germany, France, United States (although relevant forms must be filed with Federal Authorities), New Zealand (sensitive land excepted) and the United Kingdom.<sup>67</sup> RP Data states in its submission that Switzerland's approval policy is exceptions-based and New Zealand imposes certain restrictions on the ability of foreign nationals to acquire what is termed 'sensitive land'.<sup>68</sup>
- 2.57 Regulation of foreign investment in real estate in Canada is determined at a provincial level.<sup>69</sup> Canada does not have a federal approval process but several provinces have introduced a limited approval regime.<sup>70</sup> The United States has a very limited approval process which only operates in respect of certain properties.<sup>71</sup>
- 2.58 In Switzerland, foreign investors can only purchase one property as a holiday home or secondary residence and cannot rent this property long term or sell within 5 years of purchase.<sup>72</sup> RP Data notes in its submission that nationals of European Union member states living in Switzerland who have a residency permit can buy real estate but non-residents may only purchase property if it is necessary for gainful activity. Government authorisation is required for the purchase of a second or vacation home.<sup>73</sup>
- 2.59 Currently, foreign investment in Canadian residential real estate is generally unrestrained and encouraged. Overseas investors are able to purchase property if they are spending less than six months per year in Canada and the debt finance must come from a Canadian bank.<sup>74</sup> There have also been calls to improve the data collection of Canada's foreign investment approval agency.<sup>75</sup>
- 2.60 In Singapore, foreign buyers are prohibited from investing in public housing.<sup>76</sup> Only approved foreign buyers can purchase residential real estate, and must apply to the Residential Property Advisory Committee

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66 Property Council of Australia, *Submission 25*, pp. 12-14.

67 Property Council of Australia, *Submission 25*, pp. 12-14.

68 RP Data, *Submission 23*, Appendix B, p. [2].

69 Property Council of Australia, *Submission 25*, p. 4.

70 RP Data, *Submission 23*, Appendix B, p. [5].

71 RP Data, *Submission 23*, Appendix B, p. [4].

72 Property Council of Australia, *Submission 25*, p. 12.

73 RP Data, *Submission 23*, Appendix B, p. [6].

74 Property Council of Australia, *Submission 25*, p. 12.

75 Property Council of Australia, *Submission 25*, p. 4.

76 Property Council of Australia, *Submission 25*, p. 12.

for approval to purchase property.<sup>77</sup> Denmark does not allow foreign persons to purchase property without permission from the Ministry of Justice.<sup>78</sup>

- 2.61 In Switzerland temporary residents can purchase property with no authorisation required. Temporary residents can also purchase property in Singapore, Denmark, Hong Kong, Japan, Germany, France, United States, New Zealand and the UK. In Canada temporary residents are able to purchase property and they need to file tax returns.<sup>79</sup>
- 2.62 Switzerland potentially has caps on foreign pre-sales – each Canton is assigned a quota to allocate.<sup>80</sup> In Singapore, there are no caps on foreign pre-sales but a foreign person may not own all apartments within a building.<sup>81</sup> The following countries do not implement any caps on foreign pre-sales: Canada, Denmark, Hong Kong, Japan, Germany, France, United States, New Zealand, and the United Kingdom.<sup>82</sup>

## Finance and Taxation

- 2.63 The Property Council of Australia's comparison also provides information on particular taxation and financing arrangements among countries. In respect of financing investments, in Germany, banks will not give foreign buyers finance for more than 60 per cent of the purchase price of a property,<sup>83</sup> and in Japan there are limitations from banks on debt finance for non-permanent residents and a Japanese citizen guarantor is required.<sup>84</sup>
- 2.64 In regards to taxation, in Switzerland, Denmark, Japan, and New Zealand there are no special tax arrangements for foreign investors.<sup>85</sup> Non-residents are exempt from the Capital Gains Tax in the United Kingdom,<sup>86</sup> while in France buyers with an EU passport get a reduced rate of capital gains tax for each year of ownership of the property (starting at 40.5 per cent after three years). Non-EU passport holders get similar treatment

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77 RP Data, *Submission 23*, Appendix B, p. [3].

78 Property Council of Australia, *Submission 25*, p. 13.

79 Property Council of Australia, *Submission 25*, pp. 12-14.

80 Property Council of Australia, *Submission 25*, p. 12.

81 Property Council of Australia, *Submission 25*, p. 12.

82 Property Council of Australia, *Submission 25*, pp. 12-14.

83 Property Council of Australia, *Submission 25*, p. 13.

84 Property Council of Australia, *Submission 25*, p. 13.

85 Property Council of Australia, *Submission 25*, pp. 12-14.

86 Property Council of Australia, *Submission 25*, p. 14.

- (starting at 53 per cent after three years).<sup>87</sup> In Hong Kong a stamp duty refund is available if redevelopment occurs within six years.<sup>88</sup>
- 2.65 Foreign buyers in the United States are subject to 10 per cent withholding tax upon sale.<sup>89</sup> In Canada, a foreign owner must pay 25 per cent withholding tax when renting-out.<sup>90</sup>
- 2.66 Singapore currently has a 15 per cent Additional Stamp Duty for foreign investors aimed at reducing activity from speculative and potentially damaging investment rushes.<sup>91</sup> Singapore also has a withholding tax of 15 per cent that applies to interest paid to a foreign lender.<sup>92</sup> Hong Kong has a 15 per cent stamp duty for foreign buyers<sup>93</sup> and additional selling fees if properties are bought or sold too quickly by speculators.<sup>94</sup>
- 2.67 An additional stamp duty for foreign purchases of residential real estate could be considered in Australia, although this may have a considerable impact on the levels of foreign investment in this sector. The Parliamentary Budget Office (PBO) provided costings for such a regime, which are included at Appendix D. These costings show that any increased level of stamp duty would have a considerable negative impact on the market. However, these figures will require further modelling by the Treasury if additional stamp duties were to be considered in the future, say, in the process of looking at tax holistically as part of the upcoming White Paper on the Reform of Australia's tax system.

## Policies to increase housing stock

- 2.68 Of those compared by the Property Council Of Australia, the following countries do not require foreign investors in residential property to purchase new housing stock: Switzerland, Canada, Denmark, Hong Kong, Japan, Germany, France, United States, New Zealand, and the United Kingdom.<sup>95</sup> In Singapore foreign investors do not have to purchase new housing stock but they are restricted to apartments or condos approved under the Planning Act.<sup>96</sup>

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87 Property Council of Australia, *Submission 25*, pp. 13-14.

88 Property Council of Australia, *Submission 25*, p. 13.

89 Property Council of Australia, *Submission 25*, p. 14.

90 Property Council of Australia, *Submission 25*, p. 12.

91 SMATS Group, *Submission 35*, p. 10.

92 Property Council of Australia, *Submission 25*, p. 12.

93 Property Council of Australia, *Submission 25*, p. 13.

94 SMATS Group, *Submission 35*, p. 10.

95 Property Council of Australia, *Submission 25*, pp. 12-14.

96 Property Council of Australia, *Submission 25*, p. 12.

- 2.69 In Switzerland there are restrictions on foreign buyers of development sites including continuous construction commencing within one year of purchase.<sup>97</sup> There are no restrictions on foreign buyers of development sites in Canada, Denmark, Hong Kong, Japan, Germany, France, United States, New Zealand, or the United Kingdom.<sup>98</sup> In Singapore, foreign buyers cannot purchase vacant residential land.<sup>99</sup>

## Analysis

### Application of the law

- 2.70 A number of submissions to this inquiry expressed concern about the effectiveness of the FIRB approval processes for foreign purchases of residential property in Australia. Among these concerns are the purchasing of property by an Australian citizen or resident on behalf of a foreign national<sup>100</sup> and that a foreign purchase of a residential property can be somehow granted retrospective approval.<sup>101</sup>
- 2.71 There is criticism in several submissions of the pre-approvals process for developments of 100 new dwellings or more that allows developers to obtain a single FIRB approval to sell up to 100 per cent of the properties to foreign buyers (who do not then require individual approvals).<sup>102</sup> A number of reports in the media have also criticised the approval regime, describing it as a rubber stamp process<sup>103</sup> or that it is conducted in secrecy.<sup>104</sup>
- 2.72 The industry largely takes a different view of the approvals process by FIRB. Meriton Group believes that the existing approvals arrangements are working well.<sup>105</sup> The Property Council of Australia takes the view that the existing regime is adequate (but needs to be better enforced) and that

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97 Property Council of Australia, *Submission 25*, p. 12.

98 Property Council of Australia, *Submission 25*, pp. 12-14.

99 Property Council of Australia, *Submission 25*, p. 12.

100 Mr David Wong, *Submission 5*, p. 17.

101 Ms Jennifer Jaeger, *Submission 21*, p. [1].

102 Ms Anne Carroll, *Submission 13*, p. 1; Mr David Chandler, *Submission 41*, p. 4.

103 Media article <<http://www.theguardian.com/commentisfree/2014/feb/18/wealthy-chinese-buyers-are-makingsydneyshousing-problem-worse>> viewed 4 September 2014.

104 Media article <<http://www.propertyobserver.com.au/forward-planning/investment-strategy/property-news-and-insights/30041-foreign-acquisitions-and-takeovers-act-1975-order-under-subsection-21a-2.html>> viewed 4 September 2014.

105 Meriton Group, *Submission 14*, p. 1.

- the pre-approval process is important for attracting foreign investment and enabling projects to start.<sup>106</sup>
- 2.73 Nyko Property does not agree with blanket approval arrangements for overseas investors and argues that individual approvals should be required so as not to disadvantage domestic buyers.<sup>107</sup> SMATS Group expresses the view that as an FIRB application to purchase a residential property is free of charge, there are limited resources available to the Treasury to police the current regulations.<sup>108</sup>
- 2.74 The committee notes from the evidence received from the Treasury and FIRB that there have been no enforcement activities through the courts since 2006<sup>109</sup> and that only 17 divestment orders have been issued since 2003.<sup>110</sup> However, since the changes to the rules regarding foreign purchases of real estate in 2008 there have in fact been no divestment orders issued. Treasury officials could not provide any data on voluntary divestments by foreign investors, despite their assurance to the committee that they had occurred as part of their compliance program.
- 2.75 These figures are remarkably low and the committee is concerned, as mentioned earlier, that the internal processes at the Treasury, as well as the resources, are currently not adequate to properly enforce the existing rules for foreign investment in residential property.
- 2.76 The Treasury emphasises in its submission to this inquiry that there are no information sources that can be used to systematically identify non-compliant property acquisitions, nor mechanisms to prevent such transactions from proceeding.<sup>111</sup> At the public hearing on 30 May 2014, the Treasury informed the committee that case officers examine whether a foreign acquisition of an established property is lawful.
- 2.77 Mr John Hill of the Compliance and Real Estate Screening Unit, Foreign Investment and Trade Policy Division, the Treasury, informed the committee that established property applications allocated to case officers to examine 'could be in the order of 500 to 1,000 a month'.<sup>112</sup> Mr Hill stated:

We have a team of people that goes through a routine to review those cases... That process typically leads case officers to the

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106 Property Council of Australia, *Submission 25*, p. 7.

107 Nyko Property, *Submission 28*, p. [3].

108 SMATS Group, *Submission 35*, p. 9.

109 The Treasury, *Submission 31.1*, p. 1.

110 The Treasury, *Submission 31.3*, p. [4].

111 The Treasury, *Submission 31*, pp. 1, 12.

112 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 3.

Department of Immigration and Border Protection's visa entitlement verification online system, VEVO. That is basically a system that gives us three pieces of information. It confirms the identity of the individual. It tells us the category of visa the individual has and when that visa expires. It also tells us whether the individual in question is onshore or offshore. That is quite vital information to establishing who we are dealing with here.<sup>113</sup>

- 2.78 Mr Hill further informed the committee that the case officers undertake a routine consultation process:

That involves moving particular cases based on value of transaction and country of origin of the applicant to the Australian Federal Police and also to the Australian Crime Commission. We have a 30-day period in which to respond to these things under the Act. We provide a window of opportunity for consultation comments to return to us.<sup>114</sup>

- 2.79 Mr Hill added that around a third of all established property applications are registered on a watch list to indicate rental activity, noting:

It is very interesting to us to discover that a person might have received an approval to buy established property but have subsequently rented it out and disappeared or are buying something else. We will monitor around a third of our established property applications. If there is a rental trigger that we detect then we will follow that up and ask them to explain.<sup>115</sup>

- 2.80 The Treasury's submission notes that a dedicated compliance hotline has operated since 2010, from which information is used to initiate follow-up investigations. The submission advises that certain purchases identified in the media are also examined, and that information sessions with real estate agents are conducted periodically in metropolitan centres.<sup>116</sup>

- 2.81 The committee was further informed at the public hearing that the hotline is staffed from 9.00am to 5.00pm every day and receives thousands of calls. Mr Hill added:

We do spot investigations. We might see a media article. We might see a prestige property and we will go off. The process is difficult. We might have an allegation of a foreign person that has purchased the property. All we have got is an address, so we need to establish if that person is a foreign person, and that is not a

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113 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 3.

114 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 4.

115 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 4.

116 The Treasury, *Submission 31*, p. 13.

straightforward process. We will generally go to a real estate agent in the first instance and discuss what information they can tell us about the contract for sale, and the process steps from there.<sup>117</sup>

- 2.82 As noted earlier in this chapter, the committee was not provided with any precise data in relation to the operation of this hotline, and considers that detailed information on compliance activities must be accurately maintained as part of future enhancements to the internal processes at the Treasury's Foreign Investment and Trade Policy Division.

## Non-compliance

- 2.83 The committee queried the Treasury on its actions in response to non-compliance with the laws regarding foreign purchases of residential real estate. Mr Hill informed the committee that prosecution activity was very rare:

Our preference, if non-compliance is detected, is that we will seek to remedy that in consultation with the individuals and bring them back into a territory of compliance. That is our standard procedure... We try to be reasonable. If you have a situation where a foreign investor might be renting, we certainly would take into consideration a family being turfed out onto the street would not be the best outcome. So we think about what might be a reasonable time to terminate that private agreement with the tenants, who could easily be an Australian family.<sup>118</sup>

- 2.84 Mr Hill also commented on questions regarding non-compliance by temporary residents who do not sell an established property when it ceases to be their residence. He advised that there are no convenient methods for detecting such breaches but commented in relation to the monitoring of visas:

Often we could find that a person might depart in the absence of an expiry of visa... that is an opportunity to follow up on expiry of visa. We would require people to inform us about that, and we seek that from them. We have that as an opportunity that the visa system will tell us if the visa has expired. We will also talk to law enforcement agencies. In fact, they talk to us reasonably consistently. We have a compliance hotline that we operate inside the department, and that is open constantly. I do not have good data to give you, but I think it is fair to say that we would be investigating at any one time in the order of 25, 30 or 40 cases

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117 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 4.

118 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 5.

where that sort of situation might have arisen. So we are in the process of resolving that pretty much continuously.<sup>119</sup>

- 2.85 The Treasury was requested to provide figures on the incidence of non-compliance with the current regulations for foreign investors in residential real estate. In a supplementary submission to the inquiry, the Treasury indicated that no breaches had been prosecuted in the courts (as indicated earlier, there have been no prosecutions since 2006) and that investigations of foreign interests in 33 residential properties were ongoing. The Treasury states in its submission:

All of these properties are in the established residential category, with a small number involving very high value established purchases. In most instances the investigation activity involves the need to establish the identity of the relevant investor and to assess their eligibility to own the property in question.<sup>120</sup>

- 2.86 The Treasury did not provide any data on the number of investigations it had undertaken since 2006. It appears Treasury does not have this data. The Treasury emphasises in its supplementary submission that its more recent experience is that investors that have sought foreign investment approval are seeking to be compliant with the rules. The Treasury states that investors 'have been willing to work with Treasury staff to rectify any breaches, or potential breaches'<sup>121</sup> but that 'provision remains in the Act to seek penalties against investors who are not prepared to cooperate when breach situations arise'.<sup>122</sup>

- 2.87 The Treasury also states in its supplementary submission that around 340 applications from foreign investors to purchase real estate were withdrawn in 2012-13 upon advice from the Treasury that they would not be approved as they related to established properties.<sup>123</sup>

- 2.88 At the public hearing on 29 August 2014, Treasury and FIRB confirmed that there have not been any court prosecutions under the Act since 2006 and they indicated that identifying cases that could lead to such court proceedings would be a challenge. Mr Brian Wilson, Chairman of FIRB, informed the committee however that enforcement activity was still taking place. Mr Wilson stated:

I think it is worth being a little more granular about what 'enforcement' means. It can range from criminal prosecution at one

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119 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 4.

120 The Treasury, *Submission 31.1*, pp. 1-2.

121 The Treasury, *Submission 31.1*, p. 1.

122 The Treasury, *Submission 31.1*, p. 1.

123 The Treasury, *Submission 31.1*, p. 1.

end through to working with the applicants to regularise breaches, to having an applicant voluntarily dispose of a property improperly retained, to having an applicant put in a retrospective application. So to say there has been no enforcement activity is correct in terms of the prosecution component of enforcement, but there has certainly been a lot more enforcement activity, in fact, in regularising issues to bring about compliance.<sup>124</sup>

2.89 The Treasury was asked at the public hearing on 29 August to provide information on how many temporary residents had voluntarily disposed of their property, as required under the law, when it ceased to be their residence. The Treasury responded that it could not determine this from their records within the timeframe remaining for the inquiry.<sup>125</sup> The committee found this to be particularly unsatisfactory and to reflect very poor internal processes. Even with additional time, the Treasury could not supply this basic data.

2.90 Mr Jonathan Rollings of the Foreign Investment and Trade Policy Division at the Treasury emphasised at the 29 August hearing that there are different types of compliance issues but in the main they are about imposing the appropriate conditions on an approval that is sought by an investor:

I think the point I made to the committee previously was that the fact that those people have come to us for approval indicates that they are seeking to be compliant. When they may drift outside one of those conditions, we have found it productive and effective to talk to people to bring them back within those conditions. It is a separate issue if someone has bought a property who has not actually sought approval at all. We would take a different approach to someone in that category, but they are the cases that are the most difficult to identify.<sup>126</sup>

2.91 Mr Wilson assured the committee that all issues of non-compliance are taken very seriously:

I certainly do not want to leave the committee with the impression that, if faced with an example of someone who has wilfully undertaken a transaction and not sought the requisite FIRB approval, we would in some way take a soft approach and try to

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124 Mr Wilson, FIRB, *Committee Hansard*, Canberra, 29 August 2014, p. 31.

125 The Treasury, *Submission 31.2*, p. [3].

126 Mr Jonathan Rollings, General Manager, Foreign Investment and Trade Policy Division, the Treasury, *Committee Hansard*, Canberra, 29 August 2014, p. 31.

talk them around to a compliance situation. We would take the identification of any such examples very seriously.<sup>127</sup>

- 2.92 Mr Rollings commented however that due to a lack of systemic data that would enable FIRB approvals data to be checked against actual transactions (discussed further in Chapter 3), it is difficult to identify non-compliance. He remarked:

We are left to use these indirect methods to try and promote compliance as best we can. We are also promoting education, including of real estate agents, lawyers et cetera, around the requirements. But short of those methods I mentioned earlier – the compliance hotline or following up things in the media – it remains challenging to identify cases where a transaction has gone ahead that required a FIRB approval and that approval was not sought.<sup>128</sup>

- 2.93 It is of concern to the committee that the lack of any prosecution enforcement activity under the Act since 2006 may encourage a lack of compliance with the foreign investment framework as it applies to residential real estate. Strict enforcement makes a good deterrent, and is a good educator. In the committee's view, better penalty enforcement would be expected to result in fewer people attempting to circumvent the framework.

## Penalties

- 2.94 At the public hearing on 30 May, the Treasury and the FIRB Chairman explained the penalties that apply to any breaches of foreign investment rules relating to residential property. The committee was told that the maximum fine of up to \$85 000 for an individual breach by a foreign buyer of an Australian residence was a criminal penalty. There is currently no civil penalty regime under which pecuniary penalty orders can be imposed. Mr Hill commented in this regard that:

... the courts would need to be determining the appropriateness of setting those penalties. We certainly do not have administrative powers to issue fines. Of course, as most lawyers would realise, criminal intent is a very difficult thing around notification and we are dealing with people who may well not had the right information or the right advice. So those factors have a sway on the level of seriousness.<sup>129</sup>

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127 Mr Wilson, FIRB, *Committee Hansard*, Canberra, 29 August 2014, p. 35.

128 Mr Rollings, the Treasury, *Committee Hansard*, Canberra, 29 August 2014, p. 37.

129 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 5.

2.95 Mr Hill further elaborated on the penalty regime that currently operates at the Treasury in relation to foreign buyers of Australian property:

We have a range of divestment powers, where we can issue divestment orders against individuals that have acquired an interest in Australian urban land without approval. The notification powers are all about compulsory notification powers around the acquisition. Section 26 of our Act establishes technically fines and imprisonment ultimately if you do not notify. There are offences provisions for failure to comply with orders. For example, we have an order-making power in our legislation that suggests that the Treasurer can, on application or outside of an application, issue an order to either prevent the purchase or to dissolve it. Those carry similar fines and imprisonment provisions. We have a provision for the courts to enforce those orders. We have information-gathering powers in the Act. We also have—I think it is similar to part IVA in the tax Act—section 38, anti-avoidance powers. In summary, it is a criminal penalty regime that we operate in; it is certainly not a civil penalty regime.<sup>130</sup>

2.96 The committee is concerned, however, that the criminal penalty regime only applies to foreign investors personally. At the hearing, the committee sought clarity on whether any person other than the foreign investor could be subject to a penalty for a breach of the Act. Mr Hill responded:

The answer is no. The foreign person who acquires the interest is the individual that is captured by our regulatory notification system and subject to penalties. There are no penalties on lawyers and agents—et cetera. That could be a real estate agent, a migration agent or a law firm.<sup>131</sup>

2.97 A number of contributors to the inquiry comment on the current penalty regime. The Real Estate Institute of Australia (REIA), submits that ‘there has not been any public evidence of significant non-compliance despite the introduction of new measures in 2010’.<sup>132</sup> REIA comments that:

This could be for a number of reasons including; adherence by foreign investors to the requirements of the law; effectiveness of the penalties in discouraging non-compliance; a reluctance to prosecute; under resourcing and thus perhaps ineffectiveness of

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130 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 5.

131 Mr Hill, the Treasury, *Committee Hansard*, Canberra, 30 May 2014, p. 12.

132 Real Estate Institute of Australia (REIA), *Submission 17*, p. 10.

the monitoring and compliance activities of FIRB... Whatever the reasons are, individually or collectively, they are unknown.<sup>133</sup>

2.98 REIA recommends a review of the current enforcement regime to evaluate its effectiveness. Ms Amanda Lynch, CEO of REIA, commented at the public hearing on 30 May:

... if the penalties are there, they need to be enforced, which is why we advocate that a review be undertaken of the compliance and monitoring activities. We also advocate penalties in line with the value of the property as being more appropriate. The current maximum fine of \$85,000 is inadequate for multimillion dollar investments.<sup>134</sup>

2.99 At the public hearing in Melbourne on 20 June 2014, the Property Council of Australia expressed the view that a better understanding of where the problems are in the market and also of what the urban myths are is essential if considering any changes to the current penalty system. Mr Andrew Mihno, Executive Director, International and Capital Markets Division, Property Council of Australia, remarked that:

When it comes down to it, if something is not being done, if a rule is being flouted, the Property Council is in full support of making sure that any measures have sufficient impact to ensure that that would happen, if penalties are required.<sup>135</sup>

2.100 Mr Mihno was also asked by the committee for his views on developing a civil penalty system for breaches by foreign buyers of residential property. He responded:

... we also sympathise with how difficult it is to get a jury to agree to a criminal charge, especially in complex matters. We understand that in many cases a criminal case might be much harder. We would be in favour of implementing a civil penalty. Again, the usual caveats apply. If it gives an added string to the bow that enables you to monitor and enforce what is already in place, then that is a sensible measure.<sup>136</sup>

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133 REIA, *Submission 17*, p. 10.

134 Ms Amanda Lynch, CEO, REIA, *Committee Hansard*, Canberra, 30 May 2014, p. 28.

135 Mr Andrew Mihno, Executive Director, International and Capital Markets Division, Property Council of Australia, *Committee Hansard*, Melbourne, 20 June 2014, p. 13.

136 Mr Mihno, Property Council of Australia, *Committee Hansard*, Melbourne, 20 June 2014, p. 14.

**Fact Box**

- Civil penalties are based on civil rather than criminal court processes and are often aimed at preventing or punishing public harm. Criminal penalties may serve as a last-resort punishment after repeated or wilful violations.
- Criminal penalties used in Australia include fines, imprisonment and forfeiture of property. Civil penalties are often financial in nature, closely resembling fines, and often carry strict or absolute liability, in which no proof of fault or state of mind is required.
- There are no federal non-criminal penalties that include a prison sentence.
- Currently, only criminal penalties apply under the foreign investment framework.

2.101 In respect of current penalties applying only to the foreign investor in cases where a breach has occurred, Mr Mihno expressed the view that the regime could be extended to third parties who have intentionally broken the law:

As far as third parties are concerned we are in favour of there being penalties if they intentionally break the law or assist others to intentionally break the law on FIRB rules, which comes back to the whole concept of restrictive liability. It is obviously unfair to penalise a real estate agent if they do not know what is actually going on. Having said that, yes, penalties can be put in place for those people.<sup>137</sup>

2.102 Mr Bill Nikolouzakis, Director of Nyko Property, was supportive of pecuniary penalty orders under a civil regime but questioned the ability to enforce such a system. He stated:

They definitely should have a fine. I think the big issue at the moment with FIRB and buying in the existing market is not the policy, it is the policing. The policy is there. If they are buying at auction, then it is not the policy's fault, it is the policing of the policy.<sup>138</sup>

2.103 Mr Chris Curtis, Managing Director, Curtis Associates, expressed the view at the public hearing in Sydney on 27 June 2014 that a civil penalty regime was probably a good idea and that pecuniary penalty orders should relate to the value of the transaction:

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137 Mr Mihno, Property Council of Australia, *Committee Hansard*, Melbourne, 20 June 2014, p. 16.

138 Mr Bill Nikolouzakis, Director, Nyko Property, *Committee Hansard*, Melbourne, 20 June 2014, p. 23.

I think penalties should be ad valorem, in a similar way as stamp duty – \$85,000 on a \$500,000 transaction would be a complete impediment, whereas \$85,000 in a \$15 million transaction would be a fly in the ointment. If you are going to have penalties you should peg it to the asset value and make it really hurt.<sup>139</sup>

- 2.104 Meriton Group also expressed support for ‘enhanced compliance’ that would deter rule breaking and enhance public confidence in the regime submitting that:

... we are aware of concerns that temporary residents retain established dwellings after leaving the country on expiry of their visas. We understand that there is little evidence to show whether this is actually a significant problem and note that there is no reporting of compliance arrangements in the FIRB Annual Report. We consider that ongoing concerns about possible non-compliance undermine public confidence in the entire foreign investment and raise the risk of inappropriate policy responses to an established program which is making significant contributions to the national economy. We would welcome enhanced compliance arrangements for residential real estate which are commensurate with the risks involved and reported publicly as a means of boosting public confidence.<sup>140</sup>

- 2.105 At the public hearing on 27 June, in response to questions about whether there is a need to strengthen the current penalties, Mr James Sialepis, National Sales Director, Meriton Group was supportive of this possibility and commented that:

I think there needs to be a huge deterrent for people who are abusing the system, especially if it states quite clearly that they cannot buy an existing property they are purchasing – fundamentally the FIRB rules were not set up for that; it was purposely set up to help new construction – so they are obviously abusing the system and I think we should increase penalties, definitely.<sup>141</sup>

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139 Mr Chris Curtis, Managing Director, Curtis Associates, *Committee Hansard*, Sydney, 27 June 2014, p. 30.

140 Meriton Group, *Submission 14*, p. 10.

141 Mr James Sialepis, National Sales Director, Meriton Group, *Committee Hansard*, Sydney, 27 June 2014, p. 38.

## Conclusion

2.106 The current Australian framework for foreign investment in residential real estate is appropriate and is at least comparable to that in many other countries. It balances the need to enable valuable overseas investment into Australia's residential property market and at the same time ensure that the stock of housing available to Australia's citizens and residents is not diminished.

### Recommendation 1

**2.107 The Committee recommends that the current foreign investment framework applying to foreign purchases of residential real estate be retained in its current form, utilising the existing legislated prohibitions and restrictions on purchases of established dwellings, and encouraging foreign investment to increase Australia's supply of new housing.**

2.108 Improvements could be made, however, to assist the Treasury and FIRB to better monitor and enforce these existing rules. The committee is not satisfied with the internal processes at FIRB and at the Treasury's Foreign Investment and Trade Policy Division and takes the view that significant improvements need to be made in this area if the public is to have confidence in the regime governing foreign investment in residential property.

2.109 The committee is also less than impressed with the amount of compliance and enforcement data that is reported in the FIRB annual report or that could be provided to the committee under questioning. The committee considers this to be a further reflection of a deficiency in internal processes. Better processes and better data collection within the Treasury and FIRB in the future will enable better reporting and engender greater confidence among policymakers, and the public at large, that this system is beneficial and is working effectively.

## Recommendation 2

- 2.110 **The Committee recommends that the Foreign Investment Review Board and the Foreign Investment and Trade Policy Division of Treasury put in place appropriate processes for the purpose of audit, compliance and enforcement of the foreign investment framework. Such processes must accurately capture audit, compliance and enforcement data for the purpose of oversight of the Foreign Investment Review Board and the Treasury.**
- 2.111 Additional resources would enable the Treasury and FIRB to conduct more detailed audits to ensure compliance with the law and enhance public confidence that the rules are being properly enforced. The introduction of an administrative fee for all screening applications for foreign purchases could provide such resources if the revenue was hypothecated to Treasury for the purpose of audit, compliance and enforcement.
- 2.112 The level of the fee should be such that it does not significantly deter future foreign property investment. It could be determined based on the value of the transaction, such as 0.1 per cent of the property investment value, but this would be difficult to administer. A simpler administrative arrangement would be a flat fee for every application. A fee of between \$500 and \$1,500 could be considered. Costings were provided by the Parliamentary Budget Office (PBO) for fees of \$500, \$1,000, and \$1,500 and are included at Appendix C.
- 2.113 A fee regime of this nature would not only provide valuable new resources for compliance activities but also contribute greatly to data collection on completed purchases of properties by foreign investors. This fee regime would not conflict with Australia's existing World Trade Organisation (WTO) and Free Trade Agreement (FTA) obligations.

**Recommendation 3**

2.114 **The Committee recommends that the Government apply a modest administrative fee to the current screening for all foreign purchases of residential real estate, including purchases by temporary residents.**

**Fees collected should be hypothecated to the Treasury's Foreign Investment and Trade Policy Division for the purpose of funding audit, compliance and enforcement activities.**

2.115 It is notable that no prosecutions have taken place under the current criminal penalty regime since 2006. A civil penalty regime should be introduced for breaches of the regulations, which would remove the need to engage in onerous court proceedings to impose a pecuniary penalty. Such proceedings could then be reserved for cases of very serious misconduct. The difficulty associated with initiating a criminal case, and the lack of good internal Treasury and FIRB processes, has almost certainly contributed to the very small number of prosecutions.

2.116 Civil penalties should be imposed using a sliding scale based on the value of the property, so that it is not simply seen as the 'cost of doing business'. This will motivate better compliance and again, additional revenue can be hypothecated to the Treasury for the purpose of audit, compliance and enforcement.

**Recommendation 4**

2.117 **The Committee recommends that the Government introduce a civil penalty regime for breaches of the foreign investment framework as it applies to residential real estate, with the following features:**

- **pecuniary penalty orders imposed under this penalty regime to be calculated as a percentage of the property value to act as an effective deterrent; and**
- **the regime to apply to foreign investors and any third party who knowingly assists a foreign investor to breach the framework.**

**Pecuniary penalty orders collected should be hypothecated to the Treasury's Foreign Investment and Trade Policy Division for the purpose of funding audit, compliance and enforcement activities.**

- 2.118 Third parties (such as real estate agents, lawyers, or accountants) who knowingly assist a foreign investor to breach the framework as it applies to residential property should also be subject to a civil and criminal penalty.

### **Recommendation 5**

- 2.119 **The Committee recommends that the Government amend the *Foreign Acquisitions and Takeovers Act 1975* to provide that the criminal penalties for breaching the foreign investment framework as it applies to residential real estate, apply equally to any third party who knowingly assists a foreign investor in residential real estate to breach the foreign investment framework.**
- 2.120 Only foreign investors who are temporary residents have the right to purchase an established property to reside in and must sell this dwelling when they leave Australia. Under the current rules however, a foreign investor who holds an existing dwelling illegally faces no real penalty if they are caught. If an order to divest such a property or properties is made by the Government, or even if an unlawfully held property is voluntarily disposed of, the investor can keep any capital gains that result from this sale. As these gains can be substantial there is a clear disincentive to comply with the rules. Any windfall gain of this nature should be forfeited to the Government. This again will motivate better compliance and provide additional revenue that could be used by the Treasury for better auditing, compliance and enforcement procedures.

### **Recommendation 6**

- 2.121 **The Committee recommends that in any instance where a foreign owner divests an illegally held established property, any capital gain from the sale of that property be retained by the Government.**

**Funds collected by this measure should be hypothecated to the Treasury's Foreign Investment and Trade Policy Division for the purpose of funding audit, compliance and enforcement activities.**

2.122 The committee understands that while the requirement for a temporary resident to divest an established property within three months if it is no longer a primary residence is standard Treasury practice, it is not contained in Australia's Foreign Investment Policy. It is the committee's view that this standard practice should be reflected in the Policy – and as such the Policy should be amended to explicitly state this divestment time limit.

### **Recommendation 7**

2.123 **The Committee recommends that Australia's Foreign Investment Policy be amended to explicitly require a temporary resident to divest an established property within three months if it ceases to be their primary residence.**

