MERITON GROUP
Meriton Tower
L11, 528 Kent St
Sydney NSW 2000
Tel: (02) 9287 2888
Fax: (02) 9287 2777
meriton.com.au

The Hon Kelly O'Dwyer MP
House of Representatives
Parliament House
CANBERRA ACT 2600

Meriton Group
FIRB Submission

I am writing to express Meriton Group's support of the current regulations surrounding foreign investment in real estate, as detailed in our attached submission. Although offshore buyers represent only a small percentage of Australia's overall sales, this market is an important factor in maintaining business confidence and giving developers the impetus and security to embark on new projects – directly increasing the supply of new housing.

If Australia wishes to keep housing affordable and to keep developers building, it is imperative that we embrace foreign investment in real estate and the certainty it can bring to industry. In light of Australia's recent Free Trade Agreement with China, this review represents an opportunity for FIRB regulations to in fact be liberalised rather than further restricted.

It is my belief that it is a range of other factors, such as excessive local government planning requirements and fees, that add to the cost of housing and which have seen first-home buyers effectively pushed out of the market. There are many possible solutions and alternatives to this problem which do not involve restricting the flow of foreign investment in Australian real estate.

The outcomes of this inquiry are of major significance to Meriton, as the nation's largest apartment developer, and the housing market overall. In order to ensure consistent and affordable residential housing supply, it is important that Australia strengthen its ties with overseas markets that are not subject to the ups and downs of the domestic economy. Foreign investment remains a welcome source of support for the local housing and construction industries and any changes to regulation would be keenly felt. I would welcome the opportunity to discuss this issue with the Committee.

Yours sincerely
MERITON GROUP

HARRY O TRIGUBOFF A.O
MANAGING DIRECTOR

MERITON

Submission to the Inquiry into Foreign Investment in Residential Real Estate

House of Representatives Economics Committee

May 2014

Since 1963, the Australian-owned Meriton Group (**Meriton**) has been a major housing industry stakeholder and is Australia's largest builder of apartments.

The Inquiry into Foreign Investment in Residential Real Estate (**the Inquiry**) appears to be largely motivated by concerns over housing affordability and, in particular, that increasing foreign investment (due to growing middle classes in developing economies) will price domestic buyers out of the market, particularly in Sydney and Melbourne. The key argument being that demand by affluent foreign investors will outstrip the existing supply of residential properties, pushing prices higher beyond the reach of local buyers, with a major impact on first-home buyers.

Consequently, the outcomes of this inquiry are of major concern to Meriton. We strongly believe that foreign investment is critical to the continued supply of new housing to the Australian market, and that any attempts to further restrict this investment will ultimately result in adverse consequences for the supply of housing in Australia and its affordability.

SUMMARY OF KEY ISSUES

- Meriton believes the existing arrangements for seeking approval for foreign purchasers acquiring new dwellings are working well and should not be altered.
- Meriton is Australia's largest apartment builder, constructing over 2,500 new apartments annually, and accounting respectively for 6.4 per cent and 1.6 per cent of annual dwelling commencements in NSW and nationally. Our apartments may be sold, leased out, or used as serviced apartments operated by the Meriton Serviced Apartments brand.
- Currently, foreign investment provides a significant contribution to the stock of new Australian housing, increasing supply of both properties for sale and rental. This investment also contributes significantly to the local economy, adding to jobs in the building and construction industry and related supply and services sectors, and providing drive for the development of related social infrastructure. Meriton provides employment for around 2,700 people across the building and services sectors.
- Foreign investors contributed to around 13 per cent of Meriton's sales in the financial year 2012-2013, providing vital initial impetus to encourage Meriton to develop new apartment complexes. Without securing this initial foreign investment, many of Meriton's complexes may not have been developed.
- Meriton's data suggests that foreign investors are not speculators or absentee owners, but rather acquire their apartments for lease, or for use as owner occupiers (including those purchased for children studying in Australia).

- In support of government policy which is aimed at increasing the stock of new housing, Australia's foreign investment regime is already restrictive on the inflow of capital to the housing sector in comparison to similarly positioned economies.
- Housing affordability is driven by many supply and demand factors, including interest rates, land availability and costs of development (mostly subject to state policy and planning regulations, taxes and costs of labour). Foreign investment is not a significant driver of increased housing prices, playing a minor role in the overall housing market, and representing around 2.5 per cent of total annual sales.
- Foreign investment in housing also supports other government policies, such as temporary migration for workforce reasons and the development of an international market for Australian education services.
- There is a lack of publicly available data on foreign investment in residential real estate, which leads to speculative assumptions around its affect, and potentially leads to poorly informed policy changes which could inadvertently result in adverse effects on housing supply and affordability, employment and economic growth.

Section 1: Overview

Foreign investment in Australian residential real estate has often been the subject of political controversy. In the late 1980s, concerns over Japanese investment, particularly in Queensland, led to the amendment of the foreign investment legislation and the establishment of regulatory arrangements which are essentially operating unchanged today. These and the Government's view on foreign investment in residential real estate are articulated in the Australian Government's Foreign Investment Policy (**the Policy**)[1].

Under these arrangements, foreign investors must seek approval from the Foreign Investment Review Board (**FIRB**) prior to purchasing real estate in two broad circumstances. Firstly, temporary residents must seek approval if they wish to purchase a new or established dwelling for their use whilst they are legally residing in Australia for the purposes of work or study. Established dwellings must be sold when the temporary resident leaves the country. Secondly, all foreign buyers (including temporary residents and non-residents) must seek approval to purchase dwellings for purposes other than as a residence. For investment purposes, they are generally restricted to the purchase of newly constructed dwellings or vacant land for development. There are also some arrangements whereby existing dwellings can be acquired for redevelopment. There are restrictions and conditions around the timing, development, and use of these new constructions.

Australia's FIRB arrangements are restrictive compared to most similar countries. For example, there are no equivalent restrictions on foreign purchasers of real estate in the **United Kingdom** and the **United States**. **NZ** has no restrictions on housing purchases but there are some restrictions on land although these are mainly concerned with agriculture and maintaining access to significant land for Maoris.

[1] Australia's Foreign Investment Policy available at: http://www.firb.gov.au/content/policy.asp?NavID=1

In 2012-13, the FIRB approved the purchase of 11,668 dwellings by temporary residents and non-residents[2]. This is only a small number (around 2.5 per cent by number of sales) of the total residential real estate market which in 2013 had total annual sales of 468,354 dwellings[3].

It is important to remember that many foreign purchasers are temporary residents who would otherwise be seeking rental accommodation. Unfortunately, FIRB does not release data on the visa status of foreign purchasers so it is not possible to say with confidence how big this group is. However, the FIRB data does show that in 2012-13 43.7 per cent of approvals were for established dwellings – a category which is exclusively limited to temporary residents under the foreign investment rules. This is the minimum proportion of sales to temporary residents who also can and do buy new dwellings. Further, it is a common practice for the parents of students who are here on temporary residence visas to purchase accommodation for the use of their children. Unless the parents have temporary residence, or the students are buying in their own right, these purchases are restricted to new dwellings.

Thus we can see that of the 11,668 purchases in 2012-13, at least 43.7 per cent were for the use of accommodating people legally in Australia under our temporary migration arrangements. (The figure is undoubtedly much higher than 43.7 per cent but is just not publicly available.) The impact of this is that *non-resident* purchases are probably closer to one per cent of the total housing market.

Section 2: Meriton's business

Meriton has been a major provider of housing for Australians for over 50 years, having built more than 60,000 residential apartments on the east coast of Australia. As Australia's largest apartment builder, the largest home builder in NSW, and Australia's fourth largest home builder overall, Meriton now constructs around 2,500 apartments annually. These are sold, leased out, or used in Meriton's luxury serviced apartment business.

Meriton also contributes significantly to rental accommodation, providing close to 2000 residential premises across three cities, and assists buyers with property finance. In addition, Meriton is a significant contributor to Australia's tourism industry, offering more than 3,200 serviced apartments across 13 locations nationally.

Meriton's forecast turnover for 2014 is some $2 billion. In the process, it employs either directly, or as sub-contractors, up to 2,000 people in the construction industry on around 15 active building sites in Sydney, Brisbane and the Gold Coast, and over 700 in the services and tourism sector, contributing significantly to the Australian economy.

A significant amount of Meriton's participation is enabled through foreign investment, which contributed to around 13 per cent of Meriton's residential sales in 2012-13. Meriton estimates around 130 apartments have been acquired by foreign investors over the past year, with the vast majority of these leased out to local residents and held for long-term investment. Although data fluctuates, Meriton's figures show that the vacancy rates on these apartments is negligible, with up to two –thirds being leased and the remainder occupied by the owners, either for themselves or by student children.

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[2] Foreign Investment Review Board, Annual Report 2012-13.
[3] CoreLogic and RP Data (2014), Property Capital Markets Report, 2014 Issue 01.

Foreign investment into Meriton's projects has contributed to the stock of new residential housing available to Australians and we believe that continuing flows of foreign investment into new housing significantly supports the supply of residential real estate to the Australian market.

Section 3: Meriton's perspective on the terms of reference

Current arrangements

All acquisitions of residential property by temporary residents and non-resident foreign investors require FIRB approval, and are subject to various restrictions and conditions around occupancy and use. These restrictions and conditions do not apply to domestic investors.

Within this context, the government's foreign investment policy recognises the importance of foreign investment to the Australian economy, to employment, and to the development of valuable social infrastructure. It has also attempted to discourage speculation in property which would drive up house prices and adversely affect housing affordability. Consequently, the Policy deliberately encourages investment into new builds which increases the supply of residential housing and supports the building and construction industry, and discourages investment into established properties. To achieve this policy objective, the foreign investment regime differentiates between investment in new dwellings and established residential property. Investment in established residences is restricted to limited categories of investor with temporary residence rights, and is subject to conditions of occupancy and use[4].

Meriton's view is that current FIRB arrangements for new builds are already restrictive on foreign purchasers and these restrictions are more than adequate to ensure that the government's policy on residential real estate is implemented and that speculation is avoided.

Impact of current arrangements on Meriton and housing affordability

The current arrangements for foreign investment into new housing, although partially restrictive, still allow for offshore investors to participate in the Australian market, bringing significant funding which can be critical to the economic viability of a development and increasing the stock of available housing on the Australian market. For Meriton, foreign investors provide vital initial impetus to encourage us to develop new apartment complexes. Without securing this initial foreign investment, many of Meriton's complexes may not have been developed. For many other developers, that are not self-financing, securing offshore sales assists them to obtain finance for their development (financial institutions require a certain number of advanced sales before lending money for a development). Offshore buyers can fill the gap when there is inadequate demand by domestic buyers (for example when interest rates rise and Australian buyers drop off), keeping Australian developers in business. Across the market, many developments would not be possible at all without the foreign investor's advanced sales.

However, the concentration of foreign sales in any one building is limited. Bank financing conditions generally dictate that a developer cannot sell more than 25 per cent of a development to offshore investors. Although Meriton is self-financed and not subject to these restrictions, our aggregate sales have been typically around 13 per cent to offshore investors.

[4] Australia's Foreign Investment Policy available at: http://www.firb.gov.au/content/policy.asp?NavID=1

Should current FIRB arrangements around new builds be further restricted, sales would decrease, and many developers would have difficulty in raising finance. In Meriton's case, the impetus for new developments would reduce.

Section 4: Housing market considerations

Since the early 1990s, Australian dwelling prices have grown strongly, especially in our two largest cities – Sydney and Melbourne - both in absolute terms and relative to household incomes[5]. It is widely recognised[6] that the key drivers of the demand for housing and the growth in prices have been:

- demand for housing fuelled by strong population growth and growing per capita incomes, as well as high levels of aggregate employment across the economy linked to a sustained period of economic growth;
- the preference provided to housing – to both homeowners and investors - by taxation settings and by some government assistance programs such as the state-run first home owner schemes; and
- the increased capacity of Australian households, and investors, to obtain and service larger mortgages due to greater access to cheap credit.

In addition, supply factors have also contributed to the growth in dwelling prices. In particular, the availability of land for development and the cost of developing such land has been a significant constraint. Australia's Future Tax System Review[7] noted that it is not real construction costs that are driving escalating housing prices, rather it is the cost of land and land development that is the major supply-side drivers of increasing house prices.

A key determinant of the cost of supplying new dwellings, for companies such as Meriton, is the impact of state and local government zoning, planning and development approval processes. Two recent government reports – one by the Productivity Commission[8] and the other a report to the Council of Australian Governments (COAG)[9] – highlight how inefficient and unnecessary planning and development approval practices force up the costs of new dwellings.

A particular difficulty for Meriton and other developers is the combined burden of satisfying both local and State government requirements. This delays developments and adds to our costs. For example, the 2012 report to COAG identified instances where some local councils have introduced requirements that are in addition to, or exceed, state planning and development requirements, such as a minimum number of car parking spaces per new dwelling. Imposing a requirement that a developer build underground parking - which may be excess to purchasers' needs - may necessitate months of excavation, greatly adding to delays and costs.

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[5] Reserve Bank of Australia (2014) Submission to the Inquiry into Affordable Housing: Senate Economics References Committee.
[6] RBA (2004); Housing Supply and Affordability Reform (HSAR) Working Party (2012), Report to the Council of Australian Governments (COAG); and Street, A (2011) 'A House of a Home: Finding Value in Australian Residential Property', Presented to the Institute of Actuaries of Australia, 10-13 April.
[7] Australia's Future Tax System Review (2009), Report to the Treasurer.
[8] Productivity Commission (2011), Performance Benchmarking and Australian Business Regulation: Planning, Zoning and Development Assessments.
[9] HSAR report to COAG (2012).

A number of government inquiries[10] have identified the type of changes to state and local government practices and rules that would help reduce dwelling costs and improve the timeliness of the supply of new dwellings - for example, the proposal to move to code-based frameworks for assessing dual occupancy and multi-unit dwellings.

Taxation also adds significant costs, which are necessarily passed onto prices. A recent study found that in Sydney as much as 44 per cent of the price of a new dwelling is attributable to explicit and implicit local, state and federal taxes[11]. Meriton welcomes recent evidence that a number of state governments have begun to reform their planning regimes[12]. However, more is needed and an additional area for reform may be state taxes such as stamp duties.

Housing market outcomes

There have been a number of fundamental and pronounced shifts in the housing market over the last decade or so and some of these are causing concern to the community and policy makers.

Australia's very high historic levels of home ownership are declining. Australian Bureau of Statistics (ABS) figures[13] show that the proportion of Australian households that own their own home - with or without a mortgage - declined from 71 per cent in 1994-95 to 67 per cent in 2011-12. The falls in ownership are sharpest among low-income earners and those under 45.

Affordability has not worsened for most households[14]. ABS data shows that for most owners with a mortgage and private renters, housing costs, as a proportion of income, were the same in 2011-12 as they were in the mid 1990s. However, affordability is a particular problem for low-income households. The report to COAG[15] found that an increasing percentage of low income earners are unable to meet the full cost of home ownership and that the problem for some may be largely confined to a lack of means, rather than a lack of supply of dwellings. In many instances, this lack of means is compounded by casual employment making it difficult to secure finance.

As such, there is an undersupply of housing at an affordable price point for many low-income households. Unfortunately, it is likely that dwelling prices would need to be significantly lower to match some households' current budgets[16] and this in turn could have undesirable macroeconomic consequences. A recent CIE report has noted that without higher wage growth, boosted for reform and increased productivity, affordability is unlikely to improve without government and industry strategies to lower costs.

It is likely that investor demand is contributing to the recent rise in dwelling prices evident in inner city Sydney and Melbourne. However, there is no evidence that this is fuelled by foreign investors. As noted by the Reserve Bank, limits on loan sizes are less binding for property investors with

[10] HSAR report to COAG (2012); PC report (2011).

[11] Centre for International Economics (2013), Future Forecasts: Construction and Property Services Skills 2016-26.

[12] National Housing Supply Council (2013), Housing Supply and Affordability Issues 2012-13.

[13] Australian Bureau of Statistics (2013), 4130.0, Housing Occupancy and Costs 2011-12, released 28 August.

[14] ABS (2013)

[15] HSAR (2012)

[16] RBA (2014)

significant equity to deploy. In addition, such purchases also increase the supply of inner city properties available for rent.

Another pronounced trend is the shift away from free-standing dwellings. Reflecting in part state government infill targets but also changing homebuyer preferences, more than around 40 per cent of new residential building approvals are currently for medium-density or higher-density housing; compared to around one-quarter in the 1970s and 1980s[17].

The proportion of first homebuyers purchasing medium or high-density housing has also risen in response to changing preferences. However, the proportion of first homebuyers with a mortgage buying a new dwelling has been declining since the mid-1990s, reflecting the generally higher costs of new dwellings compared to existing dwellings[18]. As noted earlier in this submission, state and local governments could help ease the cost of new dwellings, including for first homebuyers, by reforming their zoning, planning and development approval practices.

In the wake of the Global Financial Crisis (GFC) developers had to focus more on pre-sales of apartments in response to the banks tightening loan conditions[19]. The Australia's Future Tax System Review[20] noted that pre-sales by developers became essential, particularly for obtaining finance for their projects. Sales to foreign investors became an essential part of the survival strategy for many developers as domestic investor activity was subdued[21] for some time due to poor rental returns and pessimism about future capital gains.

The higher state government targets to increase infill dwelling supplies, as opposed to greenfield developments, are also contributing to the expansion of pre-sales[22]. This is because greenfield developments are usually constructed in stages, reducing the peak debt exposure for developers. Hence, there is a greater need for developers to seek a high-level of pre-sales for apartment developments. In some cases, according to a 2014 study by the Australian Housing and Urban Research Institute, the minimum pre-sales requirement was 70 per cent of the estimated apartment value due to the capped loan to value ratio.

Foreign Investors

While exact figures are hard to come by, due to the lack of available foreign investment data, housing analysts, such as Saul Eslake[23], assess that it is local purchasers rather than foreign ones that are driving up dwelling prices. Most analysts agree that foreign purchasers and investors account for only a small proportion (around 2.5 per cent) of the residential market compared to domestic investors who account for almost 40 per cent of the market.

[17] RBA (2014)
[18] Australian Bureau of Statistics (2008), 4102.0 – Australian Social Trends, First Home Buyers, 23 July: ABS (2013).
[19] Rowley, S. et al (2014) The Financing of Residential Property Development in Australia, Australian Housing and Urban Research Institute (AHURI), Final Report No. 219, February.
[20] AFTS (2009)
[21] NHSC (2013)
[22] Rowley, S. et al (2014)
[23] Bleby, M. (2014) 'Boom threatens the great Australian dream of home', Sydney Morning Herald, 4 April.

At the margin, foreign purchasers may be pushing up prices in particular segments of the market such as high-quality new apartments in Sydney, Melbourne and the Gold Coast. However, even these markets are dominated by local purchasers.

Section 5: Data Analysis

The vast majority of domestic purchasers are buying established properties. New builds are a relatively small contributor to residential sales. In February 2014 the ABS estimated 43,312 established dwellings and 2,698 new dwellings were purchased under finance.[24] Assuming this ratio is similar throughout the year, this means foreign investors would only be competing with a very small subset of local home buyers.

FIRB data is particularly opaque and care must be taken in interpreting the data. Due to policy changes (which were subsequently largely reversed) *there is a significant discontinuity in the 2009-10 year thus figures from that year cannot be compared with previous or subsequent years.* Nevertheless, it is clear that total real estate approvals for purchases by foreign persons have increased significantly over the last decade from 3,848 in 2004-05 to 11,668 in 2012-13.

Temporary residents are predominantly temporary business long-stay residents and students who are legally entitled to be here and may stay for a number of years (five years is not uncommon for business visas) and need to be housed. This can be either through purchase or rental. They are allowed under the FIRB rules to buy one established property for their use as a residence and/or may also buy new property under the same rules as offshore purchasers (non-residents) who are restricted to purchases of new property.

It should also be noted that anecdotal evidence suggests that it is a reasonably common practice for offshore purchasers to buy accommodation for their children who are studying in Australia. Unless the parents have some residency status in their own right they are restricted to purchasing new property. So although the purchases may be by offshore persons, they are motivated by a need to house legitimate temporary residents.

As FIRB does not report on the visa status of applicants, there is no publicly available information on purchases by temporary residents compared to offshore purchasers. What the FIRB does provide is a breakdown of purchases of developed (i.e. established) property versus property for development (i.e. new). As discussed, the new property category includes both temporary residents and offshore purchasers, whereas the developed category is temporary residents only. The proportion of developed purchases was 47.8 per cent of the total in 2004-05 and 43.7 per cent in 2012-13.

Chart 1 shows that around half at least of all purchases are by temporary residents.

[24] http://www.abs.gov.au/ausstats/abs@.nsf/mf/5609.0

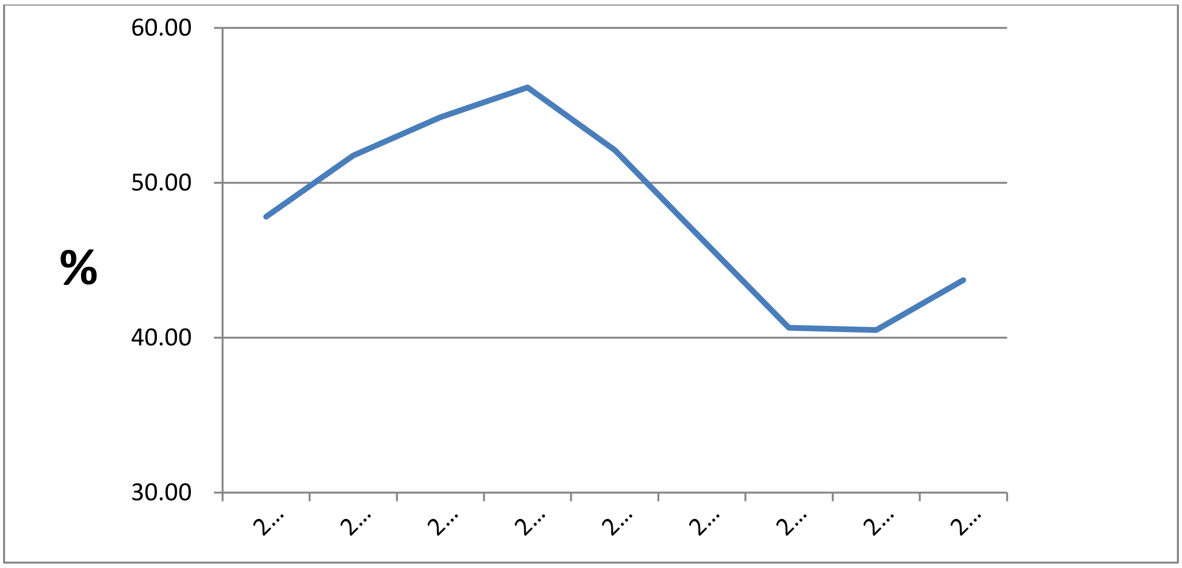

Chart 1: Established Dwellings as a proportion of all FIRB approvals, 2004-05 to 2012-13

Source: FIRB Annual Reports,
Note: 2009-10 data smoothed as average of previous and subsequent years.

There is a striking correlation between total FIRB real estate approvals and immigration data on the main two categories of temporary residents.

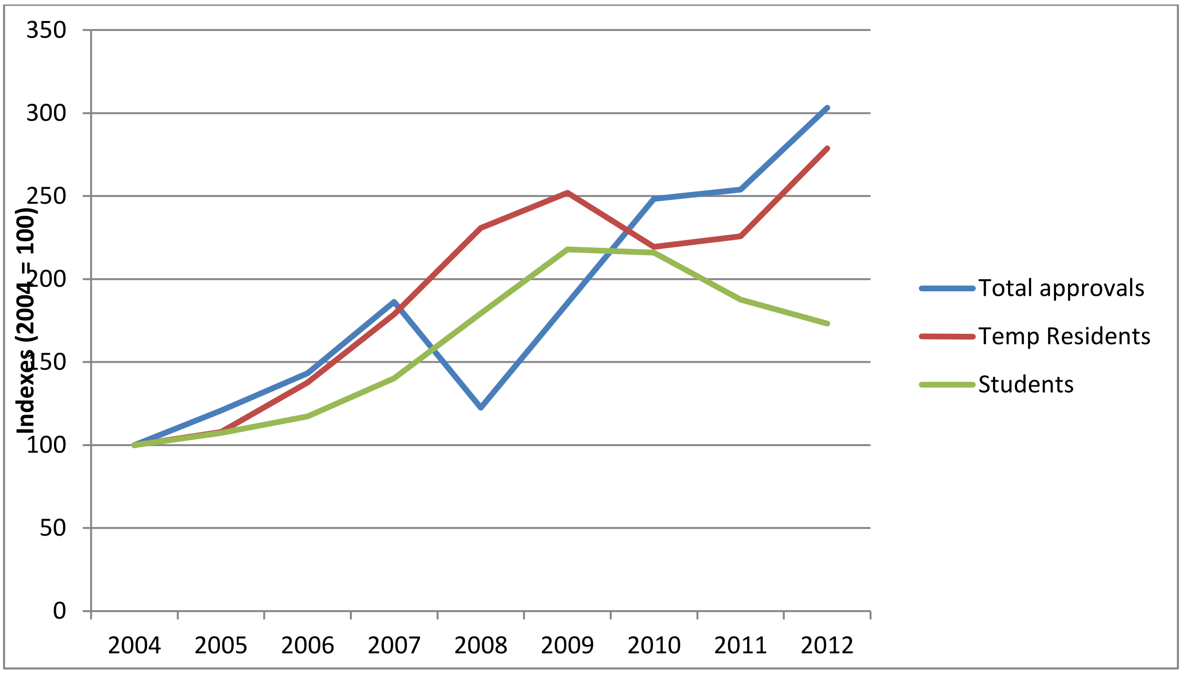

Chart 2: Residential Real Estate Approvals vs Temporary Immigration (Indexes, 2004 and 2004-05 = 100)

Source: FIRB Annual Reports and Department of Immigration and Citizenship[25]

Note: 2009-10 FIRB data smoothed as average of previous and subsequent years.
Immigration data is calendar years, FIRB data is financial years.

[25] DIAC (2013), Migration to Australia's states and territories, 2011–12.

There is no published information about numbers of foreign purchases of real estate by country of origin – rather this is reported in a table[26] where total *numbers of applications* across all FIRB categories are disaggregated into economic sectors by *dollar value*. In 2012-13 there were 622 business acquisitions, 357 commercial real estate and 11,668 residential real estate approvals. So, while precise numbers are not able to be derived, the relatively small number of non-real estate (business acquisitions) and commercial real estate approvals allow the following broad conclusions:

- China was the largest source of investment into residential real estate in 2012-13, followed by all other countries not in the top 18, then the UK, Malaysia and Singapore.
- The total value of real estate investment was $51.9 billion of which $35.8 billion was in commercial real estate. Residential real estate investment made up the remainder - $16.1 billion.
- In 2013, the actual annual number of sales in the housing market was 468,354.
- FIRB data shows that the average price paid by foreign buyers in 2012-13 for established dwellings was $1.06 million, vacant land - $763k and new dwellings - $646k. These prices are significantly above national median prices and suggest that foreign purchasers are not competing with first home buyers.

Section 6: Possible recommendations for administrative improvements

Meriton believes the existing arrangements for seeking approval for foreign purchasers acquiring new dwellings are working well and should not be altered.

However, we note that debates about foreign investment in real estate are a continuing feature of the Australian political scene and that these are exacerbated by the lack of adequate detail in the data published by FIRB. In particular, we would welcome data which shows:

- Disaggregation by visa status so that activity by temporary residents who are directly contributing to the Australian economy can be distinguished from passive investments by non-residents;
- Analysis of prices paid in different market segments;

Meriton is not a significant participant in the established real estate market but 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.

Finally, we note that much of the concern raised relates to the purported impact of foreign buyers on first-home buyers. We consider that there are significant pressures affecting first homer buyers and, while these may not be the preserve of the current inquiry, we would highlight:

[26] FIRB Annual report, 2012-13.

- The impact of state and local government regulation on the cost of bringing land on line for development;
- The potential benefits of allowing access to at least some portion of superannuation savings to assist first home buyers into the housing market, following the success of similar schemes in New Zealand, Canada and Singapore.

Section 7: Conclusions

Foreign investors are an important contributor to the stock of new housing in Australia. However, their investment is not a significant driver of increased housing prices, playing a minor role in the overall housing market.

Without their investment, many of the new apartment blocks in Sydney, Melbourne and the Gold Coast post-GFC would not have been built.

By contributing to the supply of housing, foreign investors are supporting the construction industry and employment in that industry, as well as indirectly supporting other industries and the Australian economy more broadly.

FIRB and other data does not support the argument that there is a significant problem with foreign investors forcing up prices and crowding out domestic purchasers.

Community concern about housing affordability and the low level of first homebuyers in the housing market is understandable. However, this outcome is attributable to a number of factors such as recent reductions in State government incentives for first homebuyers as well as long-standing and inefficient practices - zoning, planning development approval processes and taxes that contribute to the delay and cost of new dwellings. Community concerns are also exacerbated by the lack of transparency published by FIRB.

The current arrangements are generally working well to support government policy objectives. We have suggested some changes to improve community confidence without compromising the significant benefits from foreign investment.