The Parliament of the Commonwealth of Australia

Report on Foreign Investment in Residential Real Estate

House of Representatives
Standing Committee on Economics

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Canberra

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Chair’s foreword

The Inquiry

Residential housing has been, and will always be, an issue that is at the forefront of community debate and discussion.

Owning your own home is part of the great Australian Dream. For many it represents the opportunity to build a future, it represents connection with community and security for family.

Buying into the Australian Dream doesn’t come cheap. According to a recent International Monetary Fund (IMF) report[1], the current ratio of housing prices in Australia to average incomes is 31.6% above the historical average.

Is it any wonder then, that many Australians now worry that home ownership may be out of reach for them, for their children, or for their grandchildren? At the same time, Australians worry about rental and interest costs, and their impacts on the cost of living.

There is no one simple explanation for the decline in housing affordability – although lack of land supply, underdevelopment, state planning laws and regulations, local council red tape, and stamp duty and tax arrangements likely all play a part.

Over the years, however, many in the community have asked the question – what role does foreign investment play in residential real estate?

It was timely then that, on 19 March this year, the Treasurer, the Hon Joe Hockey MP commissioned the House Economics Committee to examine:

- the benefits of foreign investment in residential property;
- whether such foreign investment is directly increasing the supply of new housing and bringing benefits to the local building industry and its suppliers;

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1 International Monetary Fund, *House prices to income ratio: Deviation from historical average*, <https://www.imf.org/external/research/housing/index.htm>viewed 26 November 2014.

- how Australia's foreign investment framework compares with international experience; and
- whether the administration of Australia's foreign investment policy relating to residential property can be enhanced.

Current Foreign Investment Framework

Under our current foreign investment framework, as it applies to residential real estate, foreign investment is channelled into new housing so that more homes, units and apartments are built – meaning more opportunity for people to purchase. It also contributes directly to economic activity – generating employment for builders and suppliers.

When it comes to existing homes, there are generally prohibitions and restrictions. Non-resident foreign investors are prohibited from purchasing an existing home, and temporary residents (on visas of more than 12 months) can purchase just one existing home to live in while they are resident in Australia, but must sell this home on their visa expiring. All purchases, whether new or existing homes, are required to be pre-screened by the Foreign Investment Review Board (FIRB), supported by the Foreign Investment and Trade Policy Division of Treasury (FITPD).

According to FIRB statistics, in the first 9 months of this financial year, FIRB approved foreign investment into residential property of around $24.8 billion, 44 per cent higher than the $17.2 billion approved during all of 2012-13. Much of this investment is concentrated in the Melbourne and Sydney markets. Most of the increase is attributable to proposed investment in new property, which at $19.3 billion for the first 9 months of 2013-14 is 79% higher than 2012-13. The total number of established property approvals for the first 9 months of 2013-14 is 5,755 compared to 5,101 for 2012-13.

The key findings

Over six public hearings, and after considering more than 92 submissions, the committee has four key findings that translate into 12 practical recommendations.

First, there is no accurate or timely data that tracks foreign investment in residential real estate. No-one really knows how much foreign investment there is in residential real estate, nor where that investment comes from.

- A national register of land title transfers that records the citizenship and residency status of all purchases of Australian real estate would fix this and would allow facts to be injected into discussions about foreign investment, rather than 'best guestimates'. A national register would also help with compliance and enforcement with the foreign investment framework – allowing data to be compared easily.
- Other relevant government information should also be captured and made available to FIRB. At present, FIRB cannot access data from the Department

of Immigration and Border Protection on departing visa holders. Given the government has this information, this makes no sense.

- Together, these initiatives would allow authorities to track departing visa holders who may have purchased an existing home but who, under current rules, need to sell that home within three months of leaving.

Second, there has been a significant failure of leadership at FIRB, which was unable to provide basic compliance information to the committee about its investigations and enforcement activity.

- During the course of the inquiry, it came to light that no court action has been taken by FIRB since 2006. During the entire Rudd-Gillard-Rudd Government, not one divestment order was issued, which means not one government sale of illegally acquired property was made. This compares with 17 divestment orders between 2003 to 2007 when foreign investment in residential real estate was at much lower levels. FIRB was also unable to provide basic data on voluntary divestments.
- It defies belief that there has been universal compliance with the foreign investment framework outlined above since 2007.
- The systems failure at FIRB needs to be repaired; and new resources injected into FIRB to ensure better audit, compliance and enforcement outcomes.

Third, if you are not prepared to enforce the rules, then it is less likely that people will comply with the rules. This is especially true if the consequences of a breach are not meaningfully adverse.

- The ability to sanction people who have breached the foreign investment framework more easily is critical. Hence the need to bring in a civil penalty regime for breaches of the foreign investment framework; along with the need to capture those people, who have previously stood outside the framework but materially impact the integrity of our foreign investment regime. For instance, third parties who knowingly assist foreign investors to breach the rules.
- Currently, non-resident foreign investors can profit from the illegal purchase of property. Given this, the current financial penalty that can be applied to a property, regardless of its value, is seen by many as simply the 'cost of doing business'. Fines and pecuniary penalty orders should directly relate to the value of the property concerned. Furthermore investors who breach the framework should not be able to profit.

Fourth, currently the Australian taxpayer foots the bill for the administration of FIRB and FITPD, not the foreign investors applying for approval. This has arguably contributed to underinvestment in FIRB's audit, compliance and enforcement activities.

- Just as other regulators adopt a user pays model, the committee recognises that a modest administration fee can be implemented to fund enhanced audit, compliance and enforcement capacity within FIRB, as well as other new measures outlined in the recommendations.
- Parliamentary Budget Office analysis suggests that a modest application fee of $1,500 would generate revenue of $158.7 million over 4 years[2], yet amount to 0.27% or 0.20% of the purchase price for an average home in Melbourne and Sydney respectively[3].

Commitment to the Foreign Investment Framework

These practical measures will send a strong message about Australia's commitment to its foreign investment framework in practice, as well as in words.

This is important. Too often the signals in recent years have been in the opposite direction. For instance, in 2008, then Assistant Treasurer, the Hon Chris Bowen MP, removed the requirement for temporary residents to notify FIRB of all residential purchases.[4] This rule change allowed temporary residents to purchase existing homes without notifying FIRB.

Perhaps recognising that this neutered FIRB's capacity to monitor compliance with the "sale on departure" condition under our foreign investment framework, his successor, Senator the Hon Nick Sherry, reversed the change and announced a range of proposed measures to tighten monitoring and enforcement in the lead up to the 2010 election. Some of them are not dissimilar to those being recommended by the Committee. Regrettably, most of those announced measures were not pursued by his successor, the Hon Bill Shorten MP, nor any of the subsequent Assistant Treasurers in the last Government.

The Committee strongly recommends that the Government pursue the package of measures canvassed in this report.

Free Trade Agreements

Given the recent success in delivering Free Trade Agreements for the benefit of Australia, lest there be any confusion, it is important to note that residential property has never been part of any Free Trade Agreement. Accordingly, none of the recent agreements with Japan, South Korea and China impact the screening arrangements for residential property.

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[2]PBO Costings –Appendix C.
[3]Based on an average house price of $550,000 in Melbourne or $740,000 in Sydney according to [RP Data, Submission 23.3].
[4]Bowen, Assistant Treasurer, Media Release No. 107, 18 December 2008.

In conclusion

In conclusion, the Committee found that the current foreign investment framework should be retained. In practice the framework has been undermined due to poor data collection, along with a lack of audit, compliance and enforcement action by FIRB. Australians are entitled to expect that the rules are properly enforced and our committee recommendations strengthen the ability to do this.

I would also like to acknowledge and thank all of those people who have helped inform this inquiry.

In particular, those people and organisations that made submissions and presented evidence; those who sent letters and provided their views; the Parliamentary Library and the Parliamentary Budget Office for their efficient professionalism; and members of the committee, who took a very collegiate approach to this task.

Special thanks to Committee Secretary, Mr Peter Banson, Inquiry Secretary, Dr Kilian Perrem and the House Economics Secretariat team for their diligent work on this report and their willingness to assist both the Chairman and Committee Members, to enable the report to be as comprehensive as possible.

Finally, a thank you to my incredibly hardworking staff, Tania Coltman and Sarah Nicholson, for their consistently excellent work.

I look forward to the Government's response to this report and the many practical recommendations that are contained in it.

Kelly O'Dwyer MP
Chair

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Membership of the Committee

Chair	Ms Kelly O'Dwyer MP
Deputy Chair	The Hon Ed Husic MP
Members	Mr Scott Buchholz MP
	Dr Jim Chalmers MP
	Mr David Coleman MP
	Mr Pat Conroy MP
	Dr Peter Hendy MP
	Mr Kevin Hogan MP
	Mr Craig Kelly MP
	Mr Clive Palmer MP
Supplementary Member	The Hon Matt Thistlethwaite MP

Committee Secretariat

Secretary	Mr Peter Banson
Inquiry Secretary	Dr Kilian Perrem
Research Officer	Ms Marina Katic
Administrative Officers	Ms Jazmine Rakic
	Ms Sarah Tutt

Terms of reference

The overarching principle of Australia's foreign investment policy, as it applies to residential property, is that the investment should increase Australia's housing stock. The policy seeks to channel foreign investment in the housing sector into activity that directly increases the supply of new housing (such as new developments of house and land, home units and townhouses) and brings benefits to the local building industry and its suppliers.

Consistent with this principle, foreign investors are able to seek approval to purchase new dwellings and vacant land for residential development. Foreign investors cannot generally buy established dwellings as investment properties or homes; however, temporary residents can apply to purchase one established dwelling to use as their residence while in Australia.

Notwithstanding these settings, concerns are raised periodically in relation to the possible impact of foreign investment on the Australian housing market.

In this context, the Committee is asked to examine:

- the economic benefits of foreign investment in residential property;
- whether such foreign investment is directly increasing the supply of new housing and bringing benefits to the local building industry and its suppliers;
- how Australia's foreign investment framework compares with international experience; and
- whether the administration of Australia's foreign investment policy relating to residential property can be enhanced.

List of abbreviations

ABS	Australian Bureau of Statistics
ASIC	Australian Securities and Investments Commission
AUSTRAC	Australian Transaction Reports and Analysis Centre
BPM6	Balance of Payments and International Investment Position Manual, Sixth Edition
CLSA	Credit Lyonnais Securities Asia
DIBP	Department of Immigration and Border Protection
FDI	Foreign Direct Investment
FIRB	Foreign Investment Review Board
FTA	Free Trade Agreement
HIA	Housing Industry Australia
OECD	Organisation for Economic Co-operation and Development
OIO	Overseas Investment Office
PBO	Parliamentary Budget Office
RBA	Reserve Bank of Australia
REIA	Real Estate Institute of Australia
SIV	Significant Investor Visa
UDIA	Urban Development Institute of Australia
VEVO	Visa Entitlement Verification Online
WTO	World Trade Organisation

List of recommendations

Recommendation 1

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.

Recommendation 2

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.

Recommendation 3

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.

Recommendation 4

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.

Recommendation 5

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.

Recommendation 6

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.

Recommendation 7

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.

Recommendation 8

The Committee recommends that the Government, in conjunction with the States and Territories, establish a national register of land title transfers that records the citizenship and residency status of all purchasers of Australian real estate. This information should be accessible by relevant agencies from a single database.

Recommendation 9

The Committee recommends that the Government establish an alert system for the expiry of temporary visas that can be used by the Treasury to issue property divestment orders in cases of non-compliance:

- by amending the *Migration Act 1958* so that the Department of Immigration and Border Protection must inform FIRB when a temporary resident departs Australia upon expiry of their visa; and
- by establishing effective and timely internal processes at the Treasury to receive and cross-check this information against its property databases to screen for compliance with the foreign investment framework.

Recommendation 10

The Committee recommends that the Government amend the *Foreign Acquisitions and Takeovers Act 1975* to provide that residential property sold under off-the-plan certificates that is marketed for sale overseas, must be marketed in Australia for the same period of time. Breaches of this requirement should be subject to sanctions under the Act ranging from fines to the cancellation of a sale.

Recommendation 11

In light of the expected finalisation of the statutory review of the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 in early 2015, the Committee recommends that the Government consider the purchase of residential property by foreign investors as a possible area of investigation when considering amendments to the legislation.

Recommendation 12

The Committee recommends that Treasury's Foreign Investment and Trade Policy Division make greater use of the databases held by AUSTRAC, and also of other relevant Federal and State Government databases, to assist the Foreign Investment Review Board in its duties and responsibilities.