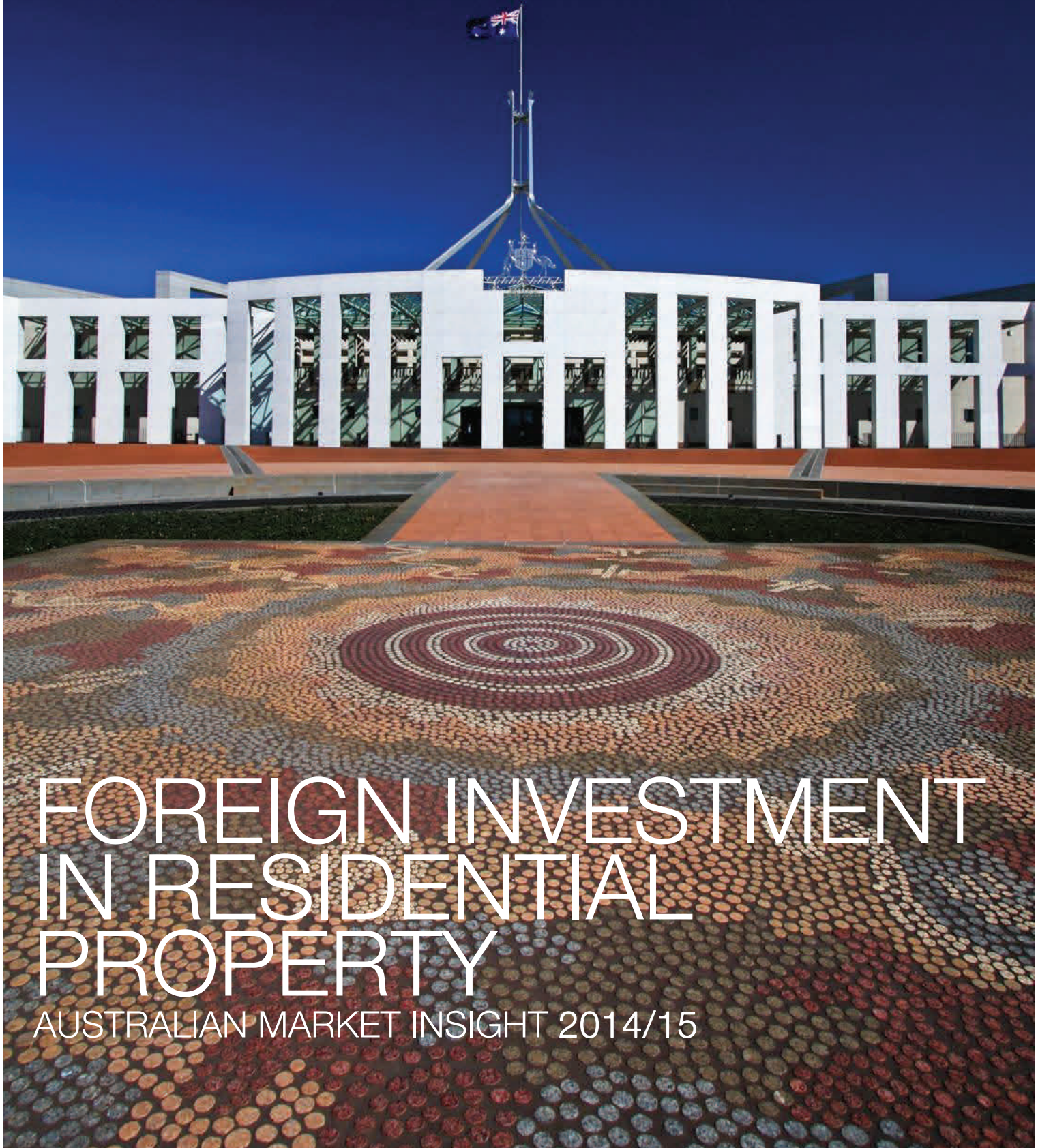


RESIDENTIAL RESEARCH



FOREIGN INVESTMENT IN RESIDENTIAL PROPERTY

AUSTRALIAN MARKET INSIGHT 2014/15

THE FINDINGS OF THE INQUIRY AND RECOMMENDATIONS BY THE HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS INTO FOREIGN INVESTMENT IN RESIDENTIAL PROPERTY IN AUSTRALIA.

KEY FINDINGS

Current FIRB regulations do not change with the recent inquiry; rather a list of recommendations have been made to make the framework more rigorously enforced

A modest administration fee to be possibly collected at time of lodging an application to purchase property

Proposition of enhanced data collection to capture additional information such as purchaser nationality

Stricter fines for purchasers and associated third parties and closer monitoring of expired visas with the Immigration Department

The idea of an additional stamp duty was floated but didn't form part of the recommendations



MICHELLE CIESIELSKI
Knight Frank Residential Research

“Being a reasonably transparent nation by global standards, how do we not know the profile of who is investing in our country and are they all abiding by the rules?”

TRACKING FOREIGN INVESTORS IN AUSTRALIA

After an eight month inquiry by the House of Representatives Standing Committee on Economics, are we any closer to understanding what role foreign investment plays in residential property?

In Australia, the current foreign investment framework for residential property is designed to generate new housing supply. The construction of new houses and apartments is aimed at increasing the opportunity for people to purchase, as well as, stimulate economic activity with the employment of builders and suppliers.

The extra supply of housing in the market, is also aimed at making home ownership more affordable, and in turn, first home ownership being attainable within the similar timeframe to that achieved of past generations. Sustained historic low interest rates, which should be an encouraging incentive alone for home ownership, have been overshadowed by the significant growth in house prices in recent years, together with the high cost of living. Higher rents continue to strain household budgets, making the desired 20% deposit difficult to achieve.

With other factors at play such as relatively high entry costs with stamp duty, the lack of new land supply and the underdevelopment in areas close to transport nodes, all contribute to the decline in housing affordability. Once you have secured your plot, the local council red tape and state planning laws and regulations are also likely to play a part in raising initial costs.

Being priced out of an auction on a weekly basis, and properties achieving well above the reserve in pockets throughout key locations of our major cities, has opened up extensive community discussion. Those attending these auctions will report back that it appeared the person that held the winning bid spoke very little English and therefore many heated debates have been had that our foreign investment

regulations needed to be reviewed.

Was this purchaser a resident? Were they bidding on behalf of someone halfway around the world? Were they an Australian citizen of more than thirty years, more comfortable in a stressful scenario speaking in their native tongue to their support team? Did the agent see the passport of the purchaser? Could this person be in breach of the foreign investment framework?

As a research house attempting to analyse foreign investment in Australia, not having access to timely, accurate information within the current framework is certainly challenging. Being a reasonably transparent nation by global standards, how do we not know the profile of who is investing in our country and are they all abiding by the rules?

In-house agencies and developers do their best to attach a survey to understand the profile of the purchasers. We know collectively the total applications seeking Foreign Investment Review Board (FIRB) approval, but the opportunity to capture the crucial details of the purchaser are often lost. This misses the opportunity to compare purchaser patterns in Australia, to those experienced around the world. More importantly, the ability to form clear views, such as, are foreign investors really pricing out local purchasers with the type of product they buy, or is the issue that the relaxing of superannuation laws created a new wave of ‘mum and dad investors’ pricing out the younger generation in the lower price bracket?

After community pressure on the Government to provide an explanation of the role foreign investment plays in residential property, on 19 March 2014, the Treasurer, the Hon Joe Hockey MP

commissioned a study to be undertaken by the House of Representatives Standing Committee on Economics (the House Economics Committee).

The House Economics Committee Were Instructed To Examine...

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

Releasing the inquiry findings on the 27 November 2014, the House Economics Committee found that the current foreign investment framework should be retained and made 12 practical recommendations to ensure there is better compliance within the existing framework. In practice, the framework has been undermined due to poor data collection, along with lack of audit, compliance and enforcement by FIRB. They stated that Australians are entitled to expect that the rules are properly enforced given that Australian taxpayers are currently paying the administration costs of the FIRB and Foreign Investment and Trade Policy Division of Treasury (FITPD).

The House Economics Committee Recommended...

- I. 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

- II. The FIRB and the FITPD **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 FIRB and the Treasury.
- III. 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 FITPD for the purpose of funding audit, compliance and enforcement activities.
- IV. 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 FITPD for the purpose of funding audit, compliance and enforcement activities.
- V. 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.
- VI. 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 FITPD for the purpose of funding audit, compliance and enforcement activities.

- VI. 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.

VIII. 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.

- IX. 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 within the foreign investment framework.
- X. 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.
- XI. 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.
- XII. Treasury's FITPD make **greater use** of the databases held by Australian Transaction Reports and Analysis Centre (AUSTRAC), and also of other relevant **Federal and State Government databases**, to assist the FIRB in its duties and responsibilities.

TIMELINE: RULES OF THE FOREIGN INVESTMENT REVIEW BOARD

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 (FIRB) 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 AUD \$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% 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 AUD \$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 AUD \$600,000 (since 8 June 1978) did not require approval.
- > Requirement of 50% Australian equity participation removed for developments that are minor (less than AUD \$10 million) or short-term in nature (less than five years to complete).

1987

- > The AUD \$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% 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% restriction could be monitored.

1989

- > *Foreign Takeovers Act 1975* renamed *Foreign Acquisitions and Takeovers Act 1975*.
- > 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% of a development with 10 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% 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.

2014/15 | CURRENT REGULATIONS

NON PERMANENT RESIDENT

- > Must apply and **gain approval from the FIRB prior to purchasing property in Australia.**
- > Applications are **generally approved if the property purchased adds to the housing stock**, including new dwellings that are yet to be occupied or sold, off-the-plan properties under construction or yet to be built, or vacant land for residential development where ongoing construction begins with 24 months.
- > **Forbidden to purchase established dwellings as investment properties or as homes.** Although there could be an exception if the established dwelling is being redeveloped into multiple dwellings, and as a result, there is an increase in the dwelling count. Over the development period, the house must remain unoccupied.

FOREIGN COMPANY WITH A SUBSTANTIAL AUSTRALIAN BUSINESS

- > Acquiring second-hand dwellings for the purpose of **providing housing for their Australian-based staff normally meet with no objections** subject to the conditions set by FIRB.
- > The company must sell the property if it is expected to remain vacant for six months or more.
- > In remote and rural locations foreign companies may rent out dwellings acquired under this category only where they are unable to sell the property.
- > Whether a company is eligible, and the number of properties it may acquire under this category, will **depend upon the scope of the foreign company's operations and assets in Australia.**
- > Foreign companies would not be eligible under this category where the property would represent a significant proportion of its Australian assets.

TEMPORARY RESIDENT

- > A temporary resident is a person who is residing in Australia and holds a temporary residency visa which permits them to stay in Australia for a continuous period of more than 12 months (regardless of how long remains on the visa); or has submitted an application for permanent residency and holds a bridging visa which permits them to stay in Australia until that application has been finalised.
- > **Are required to notify FIRB prior to purchasing property in Australia**, including an established dwelling, a new dwelling that has been purchased directly from the developer and has not been previously occupied for more than 12 months in total and vacant land for residential development where ongoing construction begins with 24 months.
- > **May acquire one established dwelling only and it must be used as their main residence (home) in Australia.** Such proposals normally meet with no foreign investment objections subject to conditions; such as, that the temporary resident sells the property when it ceases to be their main residence.
- > **Are not permitted to buy established dwellings as investment properties.**

HIGH NET-WORTH INDIVIDUAL

- > **The Significant Investor Visa (SIV)** scheme was introduced on 24 November 2012 and is operated by the Department of Immigration and Border Protection. The SIV is intended to target the migration of high net-worth individuals to Australia with the longer-term aim of transferring wealth of international businesses and individuals to benefit Australian businesses and the broader economy. Investment migrants under this scheme **are required to invest at least AUD\$5 million into complying investments in Australia for a minimum of four years** before becoming eligible for a permanent visa.
- > This process was refined during 2014/15. **A Premium Investor Visa (PIV)**, offering a more expeditious, 12 month pathway to permanent residency for those meeting an **AUD\$15 million threshold will be formally introduced on 1 July 2015.**

COMMON QUESTIONS FROM FOREIGN PURCHASERS WHEN BUYING RESIDENTIAL PROPERTY IN AUSTRALIA

Can a foreign person buy residential real estate in Australia?

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.

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

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.

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

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.

Can a permanent resident purchase residential real estate?

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

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

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

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?

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.

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.

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

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

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

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.

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

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.

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

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.

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

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.

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

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.

Can foreign investors purchase vacant land to build new housing?

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.

What happens if the regulations are breached?

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.

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

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 AUD \$85,000 for an individual (or up to AUD \$425,000 for a company), imprisonment for a maximum of 2 years, or both.

GOING FORWARD: TRACKING FOREIGN INVESTMENT IN AUSTRALIAN RESIDENTIAL PROPERTY

What data has been released by the FIRB?

Over the last two financial years, the FIRB has released the following data:

- > Approved, proposed investment for the first nine months of 2013-14 was around \$24.8 billion, 44% higher than \$17.2 billion approved during all of 2012-13. The total number of residential real estate proposals increased by 4,331 proposals to 15,999 approvals in the first nine months of 2013-14.
- > The majority of the increase is attributed to proposed investment in new property, which at \$19.3 billion for the first nine months of 2013-14 is 79% higher than the \$10.8 billion in 2012-13. Approvals for proposed investment in new property also represent the majority of the overall increase, with 10,244 approvals in the first nine months of 2013-14 compared to 6,567 approvals in 2012-13.
- > The total number of established property approvals for the first nine months of 2013-14 is 5,755 compared to 5,101 for 2012-13.
- > Approvals for foreign purchases of all real estate (commercial and residential) by country in the 2012-13 financial year were led by the United States, China and Canada; with Singapore and the United Kingdom also featuring prominently.
- > Of the total FIRB approved investment of about \$51.9 billion in Australian real estate in 2012-13, \$17.2 billion was for residential dwellings. However the residential component of foreign real estate investment was disaggregated by source country in the available data.

This data can only be used as a guide given foreign acquisitions that have bypassed the required approval process are not included in these numbers nor finalised purchases as this data represents FIRB approvals only. In many instances, several FIRB approvals are requested before a purchase is followed through.

The Findings

The key findings derived from the inquiry into foreign investment in Australian residential property, were not surprising after enduring a lengthy timeline of an inefficient framework being administered under the FIRB and lack of funding.

A national register of land title transfers that record the nationality and residency status of all purchases of Australian property would be embraced by the wider property industry.

Agencies in-house can potentially capture some of this initial data but this is normally limited to stock held on their books. Despite a lag given the nature of the data, it could be used by Government and the property industry to understand investment patterns and overlap with other data series already available.

The integration of data already captured by Immigration would greatly strengthen the dynamic database. This could allow the creation of an alert system to ensure Treasury issues temporary residents with a sale order on their departure. Otherwise the data on foreign purchases will continue to be inadequate, making policy evaluations very difficult.

Ongoing systems failure within the FIRB framework must be addressed, with additional resources essential in order to repair, then provide better ongoing audits, compliance and enforcement outcomes.

To date, the policing of foreign purchasers breaching the rules have not been enforced.

The FIRB revealed to the committee that there had not been a single prosecution since 2006 and no divestment orders since 2007. The ability to sanction people who have breached the foreign investment framework, will encourage more people to comply with the rules.

Fines and pecuniary penalty orders should directly relate to the value of the property concerned so that a profit is restricted for those in breach and discourage those who take the risk of paying the token financial penalty as simply being part of the process of doing business in Australia.

Attention has been pointed at third parties who have knowingly assisted foreigners to breach the rules. This could extend to solicitors, real estate agents, accountants and mortgage brokers. As third parties could now be liable, not just the purchaser, we may see stricter compliance with stepped up regulation.

When considering the median value of property in major capital cities of Australia, the introduction of a fee of between \$500 and \$1,500 each time the FIRB process is utilised is quite modest. By introducing this fee, the FIRB could move away from the reliance of a taxpayer funded model where the number of applications submitted are constantly fluctuating with no extra resources available to cope in peak times.

This quite logical solution could raise as much as \$158.7 million over four years and could be directly invested back into fund enhanced data capture, audit, compliance and enforcement capacity within FIRB, in addition to, new measures outlined in the 12 recommendations.



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Floating The Idea Of An Increase In Stamp Duty

The issue of an additional stamp duty for foreign purchasers was raised as an option, but didn't form part of the report's recommendations. The case studies of Singapore and Hong Kong were considered by the committee.

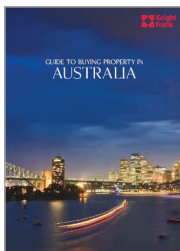
In both countries there has been a significant slowdown as a result of introducing a foreign investor stamp duty as a means of cooling the local property market. The committee tapped into the Parliamentary Budget Office (PBO) and costings were provided which showed that any increased level of stamp duty would have a considerable negative impact on the market as has been experienced in Singapore and Hong Kong.

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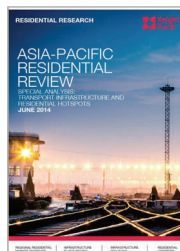
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The Recommendations

The recommendations handed down by the House Economics Committee are workable, straightforward and the first step towards making the FIRB responsible for embracing and stepping up the execution of the current foreign investment framework.

Unfortunately the recommendations are not legally binding until they are passed through the federal parliament. With the report's release so close to the tail end of 2014, any practical discussion and action within the parliamentary schedule, will be deferred to 2015.

However prior to the recommendations being handed down, there has been commitment from Treasurer Hockey that problems with FIRB would be addressed carefully, methodically and ultimately be fixed by the Government.

RESIDENTIAL RESEARCH

Michelle Ciesielski

Associate Director, Residential
+61 2 9036 6659
Michelle.Ciesielski@au.knightfrank.com

Matt Whitby

Group Director
Head of Research and Consultancy
+61 2 9036 6616
Matt.Whitby@au.knightfrank.com

RESIDENTIAL PROJECT MARKETING & KEY STATE CONTACTS

Andrew Drury

Director, Sydney (NSW)
+61 2 9036 6713
Andrew.Drury@au.knightfrank.com

Daniel Cashen

Director, Melbourne (Vic)
+61 3 9604 4749
Daniel.Cashen@au.knightfrank.com

Neil Kay

Director, Perth (WA)
+61 8 6210 0112
Neil.Kay@au.knightfrank.com

Peter McVann

Managing Director, Adelaide (SA)
+61 8 8233 5210
Peter.Mcvann@au.knightfrank.com

Scott Newton

Chief Executive Officer, Hobart (Tas)
+61 3 6220 6999
Scott.Newton@au.knightfrank.com

Matthew Knight

Managing Director, Darwin (NT)
+61 8 8982 2502
Matthew.knight@au.knightfrank.com

INTERNATIONAL PROJECT MARKETING

Erin Van Tuil

Associate Director
+61 2 9036 6699
Erin.VanTuil@au.knightfrank.com

CAPITAL MARKETS

Paul Henley

Head of Commercial Sales
+61 3 9604 4760
Paul.Henley@au.knightfrank.com

Dominic Ong

Senior Director, Asian Markets
+61 2 9036 6747
Dominic.Ong@au.knightfrank.com

