

RESIDENTIAL RESEARCH

A photograph of the Australian Parliament House in Canberra, Australia. The building is a large, white, circular structure with a central flagpole flying the Australian flag. In the foreground, there is a large, colorful Aboriginal dot painting on the ground, featuring a central sun-like motif with concentric circles and radiating lines. The sky is a clear, deep blue.

TAXING FOREIGN INVESTORS IN AUSTRALIA

RESIDENTIAL MARKET INSIGHT JULY 2016

AN ANALYSIS OF APPLICATION FEES, DUTIES AND PENALTIES FOR FOREIGN PURCHASERS WHEN BUYING, OWNING AND SELLING RESIDENTIAL PROPERTY IN AUSTRALIA

KEY FACTS

The application to purchase a new residential property across Australia must be made through the FIRB with an administration fee payable to the ATO.

Civil and increased criminal penalties are in place by the ATO for foreign investors and third parties found breaching foreign investment rules.

When buying a residential property, foreign investor stamp duty surcharges now apply in New South Wales, Victoria & Queensland.

Once a foreign investor owns a residential property, foreign investor land tax surcharges now apply in New South Wales & Victoria.

Capital Gains Withholding Tax for foreign investors has come into effect for all contracts of sale with a market value of \$2 million+. This requires 10% of the purchase price to be withheld by the purchaser and remitted to the ATO unless a clearance certificate has been provided by the vendor.



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TAXING FOREIGN INVESTORS IN AUSTRALIA

Prior to the Victorian state government introducing state-based taxes in mid-2015, foreign investors were not required to pay any additional costs to purchase an Australian residential property. One year on, foreign investors are now faced with FIRB application fees to buy an Australia property with surcharges on stamp duty and land taxes across multiple states.

In March 2014, an enquiry was commissioned for the former House of Representatives Standing Committee on Economics (House Economics Committee) to review the role foreign investment plays in Australian residential development after much-publicised pressure from local residents. After a lengthy enquiry by the House Economics Committee, in November 2014, one of 12 highlighted recommendations was the Federal Government apply a modest administrative fee to the current screening for all foreign purchases of residential real estate, after many years of the framework being undermined due to poor data collection, along with lack of audit, compliance and enforcement.

Two years on, foreign investors are faced with not only application fees when buying in Australia; but multiple state-based surcharges on stamp duty and land tax across the eastern states of New South Wales, Victoria and Queensland.

All foreign investors must now pay a FIRB administration fee before their foreign investment application will be processed and stricter penalties have been ramped up by the Australian Taxation Office (ATO) for those who breach the rules.

The current rules implemented by the Australian government are designed to encourage direct investment into the new housing market, increasing the housing supply and support local economic activity.

The application fees were only introduced to cover the administrative cost, rather than deter foreign investment into Australian residential property—but will these latest surcharges make Australia

less competitive on the global platform? There has been weighted concern from foreign buyers looking to purchase in Australia with the announcement of the increase in fees and duties, with many seeking further clarity on the new regulations.

While these additional fees and duties may deter some foreign investors, the majority of buyers investing in Australia are looking for a longer term return, such lifestyle, a place to accommodate family when studying and a transparent ownership structure—with the increased cost being absorbed as part of doing business.

It's challenging to monitor the direct impact of the foreign duty surcharge, first introduced by the Victorian State Government in mid-2015. Given foreign investors can only purchase new and off-the-plan properties in Australia; this data is only captured on settlement so the immediate impact will not be known for some time.

It also coincides with capital outflow regulation changes in China, the tightened lending on foreign investors by local financial institutions and following a lengthy and sustained period of heated residential markets in both Sydney & Melbourne.

The perception in the marketplace, including the Victorian Government at the time they announced a rise in their foreign purchaser surcharge was there was little dent in demand; with the greater concern being the tapering-off in demand after the regulation changes to outbound capital in China and banks tightening their lending practices.

THE APPLICATION TO PURCHASE A NEW RESIDENTIAL PROPERTY

- Once a property has been selected for purchase by a foreign investor, or temporary resident, an application must be submitted to the FIRB.
- The foreign investor application fee rules apply to all residential properties across Australia.
- The FIRB application must be made prior to the advance of any transaction to ensure complete legality of the purchase.
- Seeking approval from the FIRB is property-specific; therefore one application per property.
- All foreign investors must pay an administration fee to the ATO before their FIRB application will be processed.
- The fees apply for each application and is uncapped if the property is valued over AUD\$1 million as displayed in Table 1.
- If a FIRB application falls into a number of categories, the category with the highest fee would apply.
- The fee on application does not provide any assurance of securing the property.
- If a foreign person is buying into a major residential apartment project or a house-and-land package within a larger sub-division, the developer may have already gained FIRB approval for the portion of the properties they intend to sell direct to foreign purchasers. It is important to clarify this with the developer prior to purchasing an off-the-plan property.
- The ATO is now well-placed to utilise data-matching systems to identify possible breaches; an improvement on the under-resourced FIRB administration.
- When the application is submitted, the FIRB will review to ensure the property purchase will be in Australia's best interest.
- A decision on the application is generally made within 30 days—unless complications or alterations arise. If this occurs, the process may take up to 90 days.
- Stricter penalties have been ramped up by the ATO for those who breach the rules as stipulated in Table 2, on page 4.

CURRENT RULES FOR FOREIGN INVESTORS

Foreign Investors

All foreign persons, that is temporary residents and non-residents, can apply to purchase off-the-plan properties, vacant residential land for development and newly constructed dwellings in Australia.

Temporary Residents

Non-resident foreign persons are generally prohibited from purchasing established dwellings in Australia. However, temporary residents can apply to purchase one established dwelling to use as their residence while they live in Australia, although on the condition the property is sold when it ceases to be their principle place of residence.

High Net-Worth Individuals

Investment migrants under the Significant Investor Visa (SIV) 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 permanent residency. While the Premium Investor Visa (PIV) are required to invest at least AUD\$15 million into complying investments in Australia for a minimum of 12 months before becoming eligible for permanent residency; a more expeditious pathway than the SIV.

TABLE 1

Application Fees Payable by Foreign Investors, Residential Property

Based on Property Value

Value: AU\$1 million or less	Value: Over AU\$1 million
\$5,000	\$10,000 plus \$10,000 incremental fee increase per additional \$1 million in property value; uncapped.

For more detailed information, or to use the [on-line fee estimator](#), please refer to the FIRB website www.firb.gov.au

Source: Australian Government, FIRB

What are the penalties for breaching the FIRB rules?

The Australian Federal Government have recently increased criminal penalties and introduced new civil pecuniary penalties for those who breach the FIRB rules; including third party who knowingly assist foreign investors, as shown in Table 2.

TABLE 2

Penalty Regime for Foreign Investors, Residential Property

Under Foreign Acquisitions and Takeovers Legislation Amendment Bill 2015



Individual



Company

Breach of Rule	New Penalties
Foreign person acquires new property without approval > where approval would have normally been granted Temporary resident acquires established property without approval > where approval would normally have been granted	Maximum criminal penalty of: Individual 750 penalty units (AU\$135,000) or 3 years imprisonment. Company 3,750 penalty units (AU\$675,000). Maximum civil penalty is the greater of the following: 10% of purchase price in addition to the relevant application fee; or 10% of market value of the property in addition to the relevant application fee. Tier 1 Infringement Notice > Voluntary complied by coming forward. Individual 12 penalty units (AU\$2,160) plus the relevant application fee. Company 60 penalty units (AU\$10,800) plus the relevant application fee. Tier 2 Infringement Notice > Identified through compliance activities. Individual 60 penalty units (AU\$10,800) plus the relevant application fee. Company 300 penalty units (AU\$54,000) plus the relevant application fee. Note: Either an infringement notice or civil penalty would be sought, but not both.
Non-resident acquires established property or temporary resident acquires more than one established property > where not normally approved Temporary resident fails to sell established property when it ceases to be their principal residence > breach of conditional approval Temporary resident rents out an established property > breach of conditional approval Failure to complete construction within 4 years without seeking an extension > breach of conditional approval of vacant land/redevelopment	Maximum criminal penalty of: Individual 750 penalty units (AU\$135,000) or 3 years imprisonment. Company 3,750 penalty units (AU\$675,000). Maximum civil penalty is the greater of the following: The capital gain made on divestment of the property; 25% of the purchase price; or 25% of the market value of the property.
Foreign person fails to comply with reporting condition which requires them to notify of actual purchase and sale of established properties	Maximum civil penalty of: Individual 250 penalty units (AU\$45,000) Company 1,250 penalty units (AU\$225,000) Tier 1 Infringement Notice > Voluntary complied by coming forward. Individual 12 penalty units (AU\$2,160) plus the relevant application fee. Company 60 penalty units (AU\$10,800) plus the relevant application fee. Tier 2 Infringement Notice > Identified through compliance activities. Individual 60 penalty units (AU\$10,800) plus the relevant application fee. Company 300 penalty units (AU\$54,000) plus the relevant application fee. Note: Either an infringement notice or civil penalty would be sought, but not both.
Third party assists foreign investor to breach rules	Maximum civil penalty , the same as the primary breach, of: Individual 250 penalty units (AU\$45,000) Company 1,250 penalty units (AU\$225,000) Criminal penalty is: Knowingly assisting another person to commit a criminal offence is an offence under Section 11.2 of the Criminal Code (maximum penalty is the same as the primary offence).

For more detailed information please refer to the FIRB website www.firb.gov.au

Source: Australian Government, FIRB

Can the FIRB application process be streamlined by the developer of the project?

Property developers can apply for a new dwelling exemption certificate to sell new dwellings in a development of 50 or more residences to foreign investors to assist in streamlining the FIRB application process for the purchaser.

The fee for a new dwelling exemption certificate for a developer is AU\$25,000 upfront, with a reconciliation of properties sold to foreign persons based on the above rates.

What are the limits on the exemption certificate?

The Government has tightened the rules around the use of new dwellings

exemption certificates by limiting the value of all apartments that can be bought by a single foreign investor to AU\$3 million in the one development.

If foreign investors want to purchase apartments above this value, they will have to seek individual approval.

Are there any changes to the penalties for breaching the FIRB exemption certificate?

The Australian Federal Government have recently increased criminal penalties and introduced new civil pecuniary penalties for those who breach the FIRB rules.

Table 3 outlines the penalty regime for developers as stipulated under the Foreign Acquisitions and Takeovers Legislation Amendment Bill 2015.

ENHANCED COMPLIANCE AND ENFORCEMENT

- The Australian Government has initially provided \$47.5 million to the ATO (until 2019) to improve compliance and strengthen the enforcement of the rules.
- The ATO has the capacity to cover more than 600 million transactions annually through its data-matching programs.
- The ATO matches its own taxpayer data with a variety of third party sources, including FIRB, immigration, AUSTRAC, banking data and state and territory land title data.
- Suspected breaches are then followed up by around 50 investigative compliance officers.
- Investors who have breached the rules risk being identified by the ATO as part of its compliance activities. These investors (and their third party advisors) may then face criminal and/or civil prosecution.

TABLE 3

Penalty Regime for Developers, Residential Property

Under Foreign Acquisitions and Takeovers Legislation Amendment Bill 2015



Breach of Rule	New Penalties
Developer fails to market apartments in Australia > breach of new dwelling exemption certificate	Maximum criminal penalty of: Individual 750 penalty units (AU\$135,000) or 3 years imprisonment. Company 3,750 penalty units (AU\$675,000). Maximum civil penalty of: Individual 250 penalty units (AU\$45,000). Company 1,250 penalty units (AU\$225,000).
Property developer fails to comply with reporting conditions associated with approval > breach of new dwelling exemption certificate	Maximum civil penalty of: Individual 250 penalty units (AU\$45,000) Company 1,250 penalty units (AU\$225,000) Tier 1 Infringement Notice > Voluntary complied by coming forward. Individual 12 penalty units (AU\$2,160) plus the relevant application fee. Company 60 penalty units (AU\$10,800) plus the relevant application fee. Tier 2 Infringement Notice > Identified through compliance activities. Individual 60 penalty units (AU\$10,800) plus the relevant application fee. Company 300 penalty units (AU\$54,000) plus the relevant application fee. Note: Either an infringement notice or civil penalty would be sought, but not both.

For more detailed information please refer to the FIRB website www.firb.gov.au

Source: Australian Government, FIRB

BUYING AND OWNING A RESIDENTIAL PROPERTY

Duty Surcharge

Foreign investors must now pay a duty surcharge in addition to standard state-based stamp duty rates in New South Wales, Victoria and Queensland. The duty is levied on the market value of a residential property at the time of sale.

New South Wales—including the capital city of **Sydney**—has introduced a flat transfer duty of 4% applicable to all acquisitions from 21 June 2016. Additionally, foreign persons purchasing off-the-plan properties will no longer be entitled to the 12 month deferral period for the payment of stamp duty.

Victoria—including the capital city of **Melbourne**—since 1 July 2015 has imposed a duty surcharge on foreign investors at 3% of the purchase price. From 1 July 2016, this rises to 7%.

Victoria had previously held one of the lowest stamp duty taxes payable for off-the-plan properties. Stamp duty can be significantly reduced for off-the-plan properties; the amount reduced being dependant on the construction stage of the development. For off-the-plan sales, the additional duty will be calculated on

the whole of the consideration paid. Current off-the-plan concessions will still be available to foreign purchasers when calculating the normal stamp duty rate payable. Although raising the duty surcharge will effectively cancel much of the financial gain from this concession.

Queensland—including the capital city of **Brisbane** and the **Gold Coast**—a foreign investor duty will be applied at a rate of 3% for contracts signed on or after 1 October 2016; where the purchaser has a greater than 50% offshore component.

From this time, Queensland will charge the lowest duties for foreign investors buying an off-the-plan property along the East Coast, with New South Wales continuing to charge the steepest fees, although Victoria is now closing this gap. As shown in Table 5, on page 7, the case study assumes the property is purchased for investment purposes, prior to the commencement of construction.

Land Tax Surcharge

An annual surcharge is now applicable for foreign investors owning a residential property in NSW and Victoria; effective for the 2017 Land Tax year.

New South Wales—including the capital city of **Sydney**—an annual land tax surcharge of 0.75% will be enforced from Midnight on 31 December 2016; applicable for the 2017 Land Tax year to holdings of NSW residential land by foreign persons on the total land value. There will be no tax-free threshold and no principal place of residence exemption for the tax.

Victoria—including the capital city of **Melbourne**—an absentee person, considered to be a foreign purchaser not residing in the property (purchased by the foreign investor in Victoria) will be levied an annual 1.5% surcharge on the land value; from 1 January 2017 for the 2017 Land Tax year. This foreign investor land tax was first applicable in the 2016 Land Tax year at 0.5%. This foreign investor land tax is intended to minimise the number of properties that remain vacant for extended periods throughout the year; counteracting the incentive to ramp up housing rental supply.

Across Australia, no other states have introduced similar surcharges for foreign investors when buying and owning a residential property.

TABLE 4

Duties payable for Foreign Investors, Residential property

Based on Property Value, AUD, Payable in addition to standard state-based stamp duties, land taxes and FIRB application fees

	New South Wales; including Sydney	Victoria; including Melbourne	Queensland; including Brisbane & Gold Coast
Buying a Residential property			
Duty Surcharge on Purchase Price	4%	7%	3%
Applicable on or after:	21 June 2016	1 July 2016	1 October 2016
Owning a Residential property			
Annual Land Tax Surcharge on Taxable Value	0.75%	1.5%	N/A
Applicable on or after:	Midnight, 31 December 2016 for 2017 Land Tax year	1 January 2017 for 2017 Land Tax year	N/A
Further Information	www.osr.nsw.gov.au	www.sro.vic.gov.au	www.qld.gov.au/housing

Source: NSW Office of State Revenue, State Revenue Office Victoria, Queensland Government

Case Study: Comparison of Foreign Investor Duty Surcharges

TABLE 5

Foreign Investor Duty Surcharge Comparison, Residential Property

Purchase Assumptions: Foreign Investor for investment, Off-the-plan & prior to the commencement of construction, From 1 October 2016

	New South Wales; including Sydney	Victoria; including Melbourne	Queensland; including Brisbane & Gold Coast
Purchase Price	350,000	350,000	350,000
Stamp Duty	11,240	1,850 [^]	10,675
Duty Surcharge	14,000	24,500	10,500
Total Duty Payable	25,240	26,350	21,175
Purchase Price	500,000	500,000	500,000
Stamp Duty	17,990	2,265 [^]	15,925
Duty Surcharge	20,000	35,000	15,000
Total Duty Payable	37,990	37,265	30,925
Purchase Price	750,000	750,000	750,000
Stamp Duty	29,240	6,060 [^]	26,775
Duty Surcharge	30,000	52,500	22,500
Total Duty Payable	59,240	58,560	49,275
Purchase Price	1,000,000	1,000,000	1,000,000
Stamp Duty	40,490	9,605 [^]	38,025
Duty Surcharge	40,000	70,000	30,000
Total Duty Payable	80,490	79,605	68,025
Purchase Price	1,500,000	1,500,000	1,500,000
Stamp Duty	67,990	13,355 [^]	66,775
Duty Surcharge	60,000	105,000	45,000
Total Duty Payable	127,990	118,355	111,775
Purchase Price	2,000,000	2,000,000	2,000,000
Stamp Duty	95,490	21,080 [^]	95,525
Duty Surcharge	80,000	140,000	60,000
Total Duty Payable	175,490	161,080	155,525
Purchase Price	5,000,000	5,000,000	5,000,000
Stamp Duty	150,490	59,000 [^]	268,025
Premium Property Duty	140,000 [#]	N/A	N/A
Duty Surcharge	120,000	350,000	90,000
Total Duty Payable	410,490	409,000	358,025
Further Information	www.osr.nsw.gov.au	www.sro.vic.gov.au	www.qld.gov.au/housing

[^] At the date of sale, the 'Dutiable Value' is calculated by the State Revenue Office Victoria for a residential property and if applicable, varying with the stage of construction, an off-the-plan concession is deducted from the stamp duty tax payable. The large residential project used as the basis for the Victoria case study was yet to commence, had off-the-plan apartment sales ranging from \$350,000 to \$5,000,000 & was located within 3 km of the Melbourne CBD.

[#] A Premium Property Duty is payable in New South Wales when purchasing properties valued over \$3,000,000.

Important Notice: The above worked examples are an estimate only. It is highly recommended to engage a solicitor or conveyancer during the entire process of a property purchase.

Source: NSW Office of State Revenue, State Revenue Office Victoria, Queensland Government

SELLING A RESIDENTIAL PROPERTY

What changes were made to foreign resident capital gains withholding payments?

The Capital Gains Withholding Tax for foreign investors has come into effect for all contracts with a market value of \$2 million+ when signed on or after the 1st July 2016. This requires 10% of the purchase price to be withheld by the purchaser and remitted to the ATO unless a clearance certificate has been provided by the vendor. The money withheld is a portion (not in addition to) from the agreed sale price.

If a purchase price negotiated between a purchaser and vendor is on an 'arm's length basis', then the purchase price may be used as a proxy for market value.

More detailed information about foreign resident capital gains withholding payments is available at <http://www.ato.gov.au/FRCGW>

Who can be issued a clearance certificate?

The ATO can only grant a clearance certificate to a vendor who is considered to be an Australian resident. It is important to note that a residency status for tax purposes is not necessarily the same as that for immigration purposes; or for the FIRB. It is recommended to seek professional legal advice to further clarify the residency definition for this legislation slated in February 2016.

What properties does this apply to?

These changes to withholding tax apply to taxable Australian property including vacant land, buildings, residential and commercial property, leaseholds and strata title schemes.



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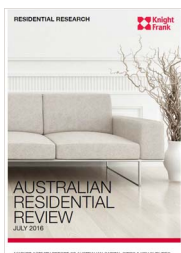
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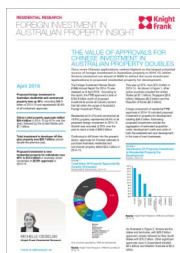
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