STRENGTHENING AUSTRALIA'S FOREIGN INVESTMENT FRAMEWORK
25 FEBRUARY 2015
CONSULTATION PAPER

Submission
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Introduction

SMATS Group is pleased to make this submission to the Foreign Investment & Trade Policy Division in response to the Governments Options Paper on Strengthening Australia's Foreign Investment Framework.

SMATS Group has submitted previous detailed submissions and made a valued contribution to this process, including the recommendation of the Foreign Buyer Fee which we are grateful to see has been given proper attention and is now a suggestion of this current paper.

We have attempted to provide a valuable insight into the various points raised in the Options Paper and feel well connected to the market most affected by these changes having been assisting Foreign Investors for 20 years through our Taxation and Finance business that operate from our Global offices in Singapore, Hong Kong, Malaysia, UAE, United Kingdom and USA.

We make this submission in the hope of contributing positively to a very important conversation that this Options Paper seeks to address.

This is a critical moment for the Australian economy as we transform from perceived mining dependency and our real estate and construction industry may well prove to be our most valuable renewable resource.

As such, the issues addressed in the Options Paper deserve full attention and we welcome any queries on the matters we have raised in response.

Yours faithfully

PROPOSED RESIDENTIAL REAL ESTATE REFORMS

Consultation Questions:

1. The government seeks feedback on the creation of a new compliance and enforcement area in the Australian Taxation Office, including:

a. Is the creation of a new compliance and enforcement area required to address concerns with foreign investment framework compliance?

Historically, the Foreign Investment Review Board (FIRB) has had the power to enforce the Foreign Investor Laws but apparent reluctance or lack of resources has meant that little or no compliance work has occurred.

The FIRB would be the logical starting point for an enforcement area, however the cost to start an important compliance program may be prohibitive.

As a Registered Tax Agent, we feel very comfortable that a compliance team located in the Australian Taxation Office (ATO) would be an improvement over the current methods and would have sufficient skills and resources (if properly empowered) to seek out abusers and remedy activity that is in contravention to the *Foreign Acquisitions and Takeovers Act 1975* (the Act).

Whether this Team in the ATO is purely investigative to find abusers and then refer the cases to FIRB, or indeed a find and prosecute division will be one to consider.

Are there alternative approaches that should be considered?

If it proves to Legislatively difficult to empower the ATO to be able to prosecute abusers of the Act, then expediency may suggest that operating the ATO division as purely a find and refer agency would allow the FIRB to focus on prosecution, while the ATO keeps resources to manage the search capability.

This may prove a more efficient model, as there will be a clear budget distinction between find and prosecute that will be easy to see and ensure that resources are not overly weighted to one or the other.

The ATO could receive man hour and resource compensation from the FIRB, funded by the proposed Application Fee and successful prosecution penalties.

The Government may also consider the creation of a Foreign Buyers "Sales Clearance Certificate" where upon the sale of any property in Australia, the conveyancer should be required to view the sellers Australian Passport or Permanent Residency Visa and if that is not available or if the seller proves to be a foreign buyer, then they need to seek the Sales Clearance Certificate from the FIRB (or the compliance team) where they can confirm that the property was legally obtained in accordance with the Act and therefor issue clearance for funds to be released to the foreign seller.

If the property had been illegally acquired, this would be clearly evident and the compliance team could be empowered to allow the sale to proceed but have the proceeds held in the conveyancers trust account until it was determined if any penalties or compliance action is required.

If this is not undertaken, then the costs to track past abusers that have sold and repatriated funds becomes extremely difficult and costly.

2. Are there other legislative impediments preventing data sharing between relevant agencies?
a. Should the Treasurer and the Australian Taxation Office have authority to obtain information, documents and evidence that relate to potential breaches of the foreign investment framework?

I am unsure of the legal issues on this matter, but any obstacles should be removed.

i. Are there alternative approaches that should be considered?

It should be remembered that many abusers of the Act may not rent the property out and as such may not be in the public view of the ATO through financial or taxation records.

It should be strongly considered that any transfer of land should require a formal acknowledgement that it is not contravening any FIRB regulation.

Many States now require a copy of passports under Identification protocols, so to check if any non-Australian passport holder has the necessary residency requirement is a small additional task that could quickly establish whether any FIRB are issues faced by the buyer.

b. Should the creation of a new compliance and enforcement area be funded by the Australian taxpayer or through the introduction of application fees on foreign investors?

Definitely any enforcement should be funded by the Application Fee so it is not a burden on the Australian taxpayer.

i. Are there alternative approaches that should be considered?

The only other alternative may be a levy on the Developer of the property, but this would place an undue burden upon them and many Developers do not seek out Foreign Buyers, so this may be an imbalance.

c. Do the proposed changes appropriately balance the need for additional scrutiny on certain foreign investment applications while continuing to streamline the process for approving investments in single developments?

If the enforcement division is kept separate from the FIRB, then it will ensure that there is no additional workload or distraction from the current approval process.

i. Are there alternative approaches that should be considered?

We do not feel any other genuine alternatives exist.

PENALTY REGIME

Consultation Questions:
The government seeks feedback on the proposed changes to the civil penalty regime, including:

a. Would a civil penalty regime be an effective addition to the rules to ensure compliance and assist with enforcement?

We strongly believe that the civil penalty regime will prove to be very effective in ensuring future compliance with the Act.

b. Are the proposed penalty amounts appropriate and likely to serve as a deterrent?

We consider the proposed penalties to be appropriate with the exception of:

- Foreign Person acquires a new property without approval,
- Temporary Resident acquires established property without approval.
- Third party assist foreign investor to breach rules

In the first two above scenarios, approval would have normally been granted, and it may be an innocent oversight or administrative error. As such the proposed 12 or 60 penalty units (individual) or 60 or 300 penalty units (company) may be too harsh and it may be considered to reduce these to a more sensible level as there has been no alteration in entitlement to ac quire, just procedural error or incompetence.

We would suggest:
Tier 1 Infringement notice — Voluntary complied by coming forward
Individual — 5 penalty units ($510) plus the relevant application fee.
Company — 10 penalty units ($1,020) plus the relevant application fee.
Tier 2 Infringement notice — Identified through compliance activities
Individual — 10 penalty units ($1,020) plus the relevant application fee.
Company — 20 penalty units ($2,040) plus the relevant application fee.

In regard to the Third Party assists penalty, we strongly consider this to be too low.

It should be noted that many Foreign Buyers innocently act on advice they receive from property professionals, accountants and lawyers. If they receive bad advice and act upon it, then the buyer may well be considered a victim rather that a perpetrator.

The advisors often may receive significant financial reward through this advice, and therefor can be compromised into allowing a transaction that is illegal to proceed.

The duty of care we should therefor expect on these advisors should be great and as such the penalty regime should be significantly higher.

The criminal penalty is sufficient, however the Civil Penalty should be increased to allow a higher maximum of 1,000 penalty units for individuals and multiplier of five for corporations.

Alternatively it could be set with the current minimum and a maximum equivalent to any remuneration received (directly or indirectly) from the facilitation of the transaction.

This sends a strong message that we seek to protect the foreign buyers as well as the Australian community from unscrupulous activity.

In all other scenarios we feel the proposed penalties to be appropriate.

c. Is the proposal to extend accessorial liability an effective way to increase compliance?

We consider the proposals very effective.

i. Are there alternative approaches that should be considered?

We feel strongly that the proposal is the best approach.

d. Is it necessary to increase the existing criminal penalties in light of the proposed new civil penalties?

We do not feel it necessary to increase the current criminal penalties provided that a civil and criminal penalty can both be brought upon wrong doers.

EXTENDING CIVIL PENALTIES AND INFRINGEMENT NOTICES TO BUSINESS APPLICATIONS

Consultation Questions:

4. Should the new penalty regime be extended to business, commercial real estate and agricultural applications?

We do not have great expertise in this area, but feel the proposed changes are fair and reasonable and a similar penalty regime should apply to business as well as real estate.

A similar harder stance suggested for Real Estate applications on the third party assisters should apply.

INTRODUCING FEES ON FOREIGN INVESTMENT APPLICATIONS

Consultation Questions:

5. The government seeks feedback on the introduction of fees on foreign investment applications, including:

a. Should the Government charge application fees on foreign investors to fund screening, compliance and enforcement activities?

There is no doubt that an application fee is appropriate and a prudent step.

It was first mentioned in our Submission to the House of Representatives and we stand by our initial recommendation and applaud the Government for taking the courageous and necessary decision to introduce the fee.

i. Are there alternative approaches that should be considered?

It would appear the only alternative to an application fee would be:

- The Government to cover the cost of compliance from general revenue, or
- A Levy on the construction industry.

Either of these two options seem inappropriate.

The first one is improbable as the lack of financial resources has led to the current problem, with FIRB having little or no compliance activity. In addition, the perilous state of the Federal Budget would seem that there is little likelihood of finding the required funding from current financial resources.

A Levy on the Construction industry would be an unwelcome impost and another layer of administration which would make it cumbersome and problematic to maintain. It would also be difficult to ensure financial fairness across the industry as not all developers engage with Foreign Buyers.

As such, an Application Fee should be the only approach considered.

ii. Should there be any exceptions to paying the application fee?

We do not believe that there should be any exceptions to paying the fee.

The Act is currently very clear who needs to submit an Application, and the fee should be payable for all submissions to the FIRB.

b. Is the level of the fees appropriate?

The proposed fees are definitely on the higher range of the spectrum.

In our original submission, we suggested a fee structure of

- A$2,000 for acquisitions under A$500,000, and
- A$3,000 for acquisitions over $500,000

The proposed fee starting at $5,000 is no small sum, and given that in 2012-13 there were 11,668 residential and 357 commercial property applications this would have resulted in over $6m in collections.

There has been no mention of the costs of running a compliance program, and the application fee should be estimated to raise sufficient revenue to ensure that any compliance program is fully funded, so the decision on the value of the fee should have some bearing based on the cost recovery required.

At $5,000 there will no doubt be a backlash from the Foreign Buyer market and resistance to a new cost of acquisition in the Application fee.

As has been outlined in the Options Paper, other countries have similar an indeed higher cost impositions on Foreign Buyers, so the concept is not unusual to the experienced investor.

The danger for Australia is our genuine need to maintain a consistent level of Foreign Investment to provide additional housing stock and critical economic activity in the construction sector.

This higher end Application Fee coupled with the changes to Capital Gains Tax introduced in May 2012 to Foreign Buyers may cumulatively have a significant negative impact on Australia's reputation as a welcoming investment destination.

It remains our strong contention that the introduction of the Application Fee should be partnered with the following initiatives:

Reinstatement of the 50% CGT Concession for Foreign Buyers and Expatriates

The removal of this CGT concession in May 2012 was not only unfair and unnecessary, but has created a high level of complexity and confusion.

We remain of the opinion that this change was erroneous and needs to be repealed as soon as possible.

Foreign Investors need to be encouraged to take a long term position in Australia, as short term speculation can be damaging to the housing industry and economy generally.

The reinstatement of the 50% discount could be allowed on the basis that any Foreign Investor that does not hold Australian Citizenship or Permanent Residency will only be entitled to the 50% CGT discount if the asset is held more than 5 years (rather than the 12 month requirement for Australian Citizens and residents).

This would ensure that the economic value of their investment can have real and permanent positive impact on the economy and ensure and short term, speculative investment was either discouraged or appropriately taxed.

By re-introducing this measure, we send a clear message that we are genuinely seeking long term Foreign Investment and only bringing in the Application Fee to cover administrative costs to ensure the property industry remains safe and protected in accordance with current legislation.

Reinstatement of the 50% Maximum Foreign Sales Quota per Development

The current ability to sell an entire project to Foreign Buyers is not in the interests of Australia.

It allows projects to be undertaken that do not consider the needs of the local market and we have seen a distortion to undersized dwellings and inconsistent price ranges.

This has a long term detrimental impact on both the market and reputation of Australia as an investment destination.

The market is affected by having higher levels of new property supply in areas of low demand (small apartments) while the larger demand areas (multi person dwellings and housing) tend to be undersupplied. This distortion places additional pressure on the housing balance.

History has shown that high priced, low demand property has poor resale growth potential with higher risk of loss on investment. When Foreign Buyers invest in Australia for poor or negative gains, they quickly communicate that to other investors and the flow of funds slows significantly.

This is especially true when a new cost is introduced such as the application fee suggested. Investors will naturally assess al costs of acquisition against the potential for gain, and only where they consider this to be probable of recovery will they proceed.

It is essential that Government Policy protects our industry from bad practise and ensures our reputation as a safe and reliable property investment destination is maintained.

The requirement for all developments to sell a minimum of 50% of their offering in the local market is a natural protection as they must assess and deliver property options that are genuinely required by the locals, thus relieving supply pressure and improving stability of necessary supply to meet the increasing demand.

Limit Significant Investor Visa (SIV) Holders to New Property

This special Visa class should have a condition of only new property acquisition.

Unlike a Temporary Visa, which expects a more permanent, albeit temporary, stay in Australia, the SIV has been appropriately designed for those more affluent foreigners that may only spend short periods in Australia.

As such this Visa only requires 40 days per year for renewal. Given this, it may be more appropriate to ensure that any residential property they acquire be for newly built rather than established, to further ensure that their economic impact on the Australian economy is maximised.

The above changes will ensure the proposed value of the Application Fee is fair and achieves the desired result of protecting the property sector and adequately policing it for the benefit of all Australians while creating a strong and continuous Foreign Investment flow that is crucial to the construction industry.

i. Will the fees act as a barrier to foreign investment?

From our significant experience, the proposed fee will not be a barrier to foreign investment, especially when combined with our other recommendations above.

The key issue is how the new Application Fee is perceived.

Some level of appropriate education is required to ensure that Foreign Buyers know that there have been no changes to the rules in which they can buy property. This fee is to police activity and ensure that it is in accordance with the Act and hence provide a safer and fairer investment climate for all.

If this message can be properly communicated, then the nature and size of the Application Fee will become and accepted cost of Acquisition.

ii. What might be the cumulative impact on business reinvestment?

The Application Fee from a Business perspective should have little impact on reinvestment.

The proposed fees for Business seem very moderate for modern times and should not act as any deterrent to investment and/or reinvestment in Business sectors.

c. What options should be considered to ensure applicants that submit multiple applications (for example, bidders at auctions or business applicants that withdraw and resubmit) are not charged excessive fees?

It would be very simple for Foreign Investors requiring in advance consent from the FIRB could be given an "Acquisition Certificate" that allows them to bid at unlimited auctions, but only acquire one property.

Any property Auction or bidding process should require the seller to establish the residency requirement of the buyer buy confirming their residence or viewing this certificate.

The certificate could be presented to an Auctioneer upon successful bidding and retained, therefor not allowing the Foreign Buyer to move to a subsequent Auction unless he has an additional certificate.

If the Certificate may be returned to FIRB for refund if not used, ensuring the applicant only pays one Application Fee to obtain the certificate, which is refundable on surrender if he cannot find an appropriate property.

ADVANCED OFF-THE-PLAN CERTIFICATES

Consultation Questions:

6. The government seeks feedback on the proposed changes to advanced off-the-plan certificates, including:

a. Should penalties be introduced for developers that fail to comply with obligations to market domestically?

We do not believe it is necessary to introduce penalties in these circumstances.

There is little proof that this area is being abused and in truth, it is very difficult to sell 100% of any development overseas to multiple buyers.

There is also difficulty in defining what marketing should be. Is a sign on the site sufficient marketing or does it need specified press advertising?

Our recommendation to reduce the Foreign Buyer Quota to the previous level of 50% would be a more appropriate way to stop perceived abuse in this situation.

i. If so, what should developers be required to do to prove they have marketed domestically?

It is difficult, and maybe impossible, to define this. Conversation, on site display, mere mentioning to an agent would supposedly qualify as a level of marketing and some of these instances have no proof element.

The merit of proving local marketing is cumbersome and problematic and a 50% Foreign Buyer sales quota is a stronger policing element.

ii. What level of penalty would be appropriate for developers that fail to comply with obligations to market domestically?

No penalty is recommended.

iii. Are there alternative approaches that should be considered

Reinstatement of the 50% maximum sales to Foreign Investors is a more appropriate solution.

IMPLEMENTATION OF AGRICULTURE COMMITMENTS

Consultation Questions:

7. Should the definition capture all primary production businesses as well as certain first stage downstream businesses beyond the farm gate (for example, meat processing, sugar milling and grain wholesaling / storage / milling)?

8. If it is decided that the ANZSIC codes be used, which divisions (or sub-divisions, groups) of the ANZSIC codes should be included in the definition for 'agribusiness'?

9. Is there an alternative approach that should be considered to define agribusiness?

10. The government seeks feedback on the proposed definition for 'agricultural land':

a. Is the proposed definition of 'agricultural land' consistent with common understanding of the term?

i. Are there alternative approaches that should be considered?

b. Would the proposed definition provide sufficient clarity as to what constitutes 'agricultural land' for the purposes of Australia's foreign investment framework?

This is not an area within our expertise so we cannot contribute with authority ion this matter.

That said, we have great concerns over the sovereignty of Australia's rural land and especially the control and management of our water resources.

Any Foreign Investor Policy on rural land needs to look at best practise and long term protection of valuable water and top-soil resources that are often abused in offshore farming practices.

The conversation needs to encompass the ownership and management of rural land as a package, not as independent issues.

DEFINITION OF 'URBAN LAND'

Consultation Questions:

11. The government seeks feedback on the proposed definition of urban or 'residential land', including:

a. Is the proposed definition of 'residential land' consistent with a common understanding of the term?

i. Are there alternative approaches that should be considered?

b. Would the proposed definition provide sufficient clarity as to what constitutes 'residential land' and related subcategories (such as new and existing dwellings) for the purposes of Australia's foreign investment framework?

We feel that the proposed definition of "residential land" is satisfactory, simple and clear tom understand.

As such, no other alternative need to be considered.

‘OTHER LAND’

Consultation Questions:

12. The government seeks feedback on three possible options for the screening of ‘other land’:
a. ‘Other land’ be defined as all land that is not ‘agricultural land’ or ‘residential land’ and continues to be screened from dollar zero;
b. ‘Other land’ is not defined and any land that is not ‘agricultural land’ or ‘residential land’ no longer requires foreign investment approval; or
c. ‘Other land’ is defined as a subset of what is left over from ‘agricultural land’ or ‘residential land’ capturing land that remains of interest while excluding some land from screening.
i. If option c is pursued, what types of land should continue to be screened?

The concept of other land needs to be carefully considered to assess the future impact of changes in zoning. For example, land that may currently be of commercial use (ie factory) that may be able to also be used for a future residential development should zoning be changed.

This may not be of any significant consequence, as a Foreign Investor buying commercial property is generally exempt from FIRB approval (subject to thresholds) and would ordinarily be approved to acquire land for development, albeit permission would need to be sought.

AGRICULTURAL LAND REGISTER

Consultation Questions:

13. The Government seeks feedback on implementation issues around the foreign ownership of land register, including:
a. the foreign ownership details that would be published and collected by the register;
b. the two-stage implementation approach to information collection (through self-reporting then through state and territory land titles processes); and
c. how lawyers or register conveyancers would verify whether their client is a foreign person?

We strongly support the establishment of a register of foreign landowners.

The process would be best managed by lawyers or conveyancers at the time of title transfer and could be managed by State Land Departments quite easily within the current requirements.

Much of this information is available through Land Tax record keeping now, however there may be a need to expand or improve the current recording procedures or technology.

MODERNISING AND SIMPLIFYING THE FOREIGN INVESTMENT FRAMEWORK

Consultation Questions:

14. The Government seeks feedback from interested stakeholders on options to modernise and simplify the Act, Regulations and Policy and streamline interaction between applicants and the Foreign Investment Review Board.

15. Are there harmonisation opportunities with other Acts (e.g. the operation of the Insurance Acquisitions and Takeovers Act 1991 or the Financial Sector (Shareholdings) Act 1998? Should the definition of 'Associate' in the Act conform with the definition of 'Associate' in the Corporations Act 2001?)

16. Is the current regime for enforcement of FIRB conditions effective? What alternative measures could be considered?

17. Should FIRB provide specific regulatory guidance on approaches to applications and difficult interpretation issues like the Australian Securities and Investments Commission and the Takeovers Panel do?

Our expertise relates to residential real estate and in that sector, the Act and FIRB guidelines are clear and do not need improvement or modernisation.

We feel strongly that the rules protect Australia's economic and proprietary interests and safeguard our citizens from direct competitive threat of foreign investors.

The issue is not with the policy, rather the policing of the Act and that is where the attention needs to be focused for any changes that may be proposed.

If foreign investors are permitted, and indeed encouraged by some wayward advisors, to find loopholes and blatantly disregard the well established law, then we need a strong body that will seek out wrong doers and prosecute with authority.

There is no doubt Australia will remain an attractive investment destination, and we need to adequately provide appropriate housing for our growing population, so the beneficial role that foreign investors play in our market should not be ignored or disrespected.

If we continue to welcome foreign investors under the well accepted and well performing rules of the current Act, then Australia can benefit for decades from the valuable economic activity and housing expansion that genuine foreign investors provide through acquisition of newly constructed property.

The billions of dollars of direct investment and subsequent multiplier effect need to be carefully considered, as does the perception of how changes should be managed.

The introduction of an Application Fee without a clear statement of how we encourage foreign investment through the creation and maintenance of a safe investment environment, could have a devastating effect on our global reputation and willingness for the current levels of foreign investment to continue.

If the fee was coupled with a potential return to investor equality through the repeal of the CGT discount removal laws then this would send a statement that we value long term investment and offer global investors a safe haven in an otherwise volatile world. This would resonate loudly and ensure we maintained or improved our foreign investor activity for the economic benefit of the country.