

Managing Compliance with Foreign Investment Obligations for Residential Real Estate

Australian Taxation Office
Department of the Treasury

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Canberra ACT

19 June 2018

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken an independent performance audit in the Australian Taxation Office and the Department of the Treasury titled *Managing Compliance with Foreign Investment Obligations for Residential Real Estate*. The audit was conducted in accordance with the authority contained in the *Auditor-General Act 1997*. I present the report of this audit to the Parliament.

Following its presentation and receipt, the report will be placed on the Australian National Audit Office's website—<http://www.anao.gov.au>.

Yours sincerely

Grant Hehir
Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

AUDITING FOR AUSTRALIA

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Summary and recommendations

Background

1. The Government's policy for foreign investment in residential property is to channel foreign investment into new dwellings to support additional jobs in the construction industry as well as economic growth.¹ Foreign investment applications are considered in light of that policy and the overarching principle that the proposed investment should increase Australia's housing stock.
2. Foreign investors are required to receive approval before acquiring an interest in residential real estate. Taking an interest in residential real estate prior to receiving approval is a breach of the *Foreign Acquisitions and Takeovers Act 1975*. Australia attracts a large volume of foreign investment applications for residential real estate, with 40 149 applications in 2015–16, and approvals that year totalling \$72.4 billion in proposed investments.
3. In the 2015–16 Budget, the Government announced a package of measures aimed at strengthening Australia's foreign investment framework. The package was introduced in response to a:
 - Senate committee inquiry report in 2013, *Foreign Investment and the National Interest*, which included 29 recommendations; and
 - House of Representatives committee 2014 *Report on Foreign Investment in Residential Real Estate*, which included 12 recommendations.
4. Subsequent to the two reports, responsibility for residential real estate under the foreign investment framework was transferred from the Department of the Treasury (Treasury) to the Australian Taxation Office (ATO), including the collection of fees, upfront screening, compliance and enforcement. Further, the ATO was responsible for establishing a register of foreign investment in agricultural land and residential real estate.

Rationale for undertaking the audit

5. The Australian National Audit Office (ANAO) selected foreign investment in residential real estate for audit because of the extent of parliamentary and public interest in the issue, including concerns that foreign investors were not complying with foreign investment obligations and purchasing properties they were not entitled to own. The audit would also indicate the impact on compliance with foreign investment in residential real estate arising from the change in administrative arrangements.

Audit objective and criteria

6. The audit objective was to assess the effectiveness of the ATO's and Treasury's management of compliance with foreign investment obligations for residential real estate.

1 Foreign Investment Review Board, *Guidance Note 1*, p. 1, available from <http://firb.gov.au/resources/guidance/gn01/>, [accessed 2 May 2018].

7. To form a conclusion against this objective, the ANAO adopted three high level criteria:
- compliance and enforcement strategies and detection arrangements were in place to support compliance activities;
 - activities were undertaken to promote voluntary compliance and effectively address identified instances of potential non-compliance; and
 - the effectiveness of compliance arrangements was monitored and reported.

Conclusion

8. The ATO's management of compliance with foreign investment obligations for residential real estate is becoming effective as it progressively implements more sophisticated approaches to encourage compliance and detect and address non-compliance.
9. The ATO has developed processes for compiling a land register of residential real estate but faces considerable challenges in populating the register with reliable data in coming years, which it needs to overcome in order to be effective.
10. The ATO has assessed and addressed compliance risks in relation to foreign investment obligations for residential real estate but has not yet compiled and implemented a compliance and enforcement strategy. To promote voluntary compliance with those obligations, the ATO has developed a series of communication strategies. The strategies, which have largely been implemented, incorporate a multi-platform communication approach targeting key audiences with priority messages.
11. The ATO has undertaken a significant amount of work to develop processes and systems to support the detection and investigation of non-compliance with foreign investment obligations for residential real estate. There are a number of minor enhancements the ATO could make to improve its largely effective investigation processes, with more substantial work required in its development of processes to actively detect non-compliance.
12. Monitoring and reporting on compliance activities for foreign investment in residential real estate has been expanded with the transfer of responsibilities from Treasury to the ATO. Many indicators have been developed to measure the success of compliance activities and external reporting established for compliance investigations, outcomes and penalties. The monitoring and reporting arrangements are largely effective, and could be strengthened by more broad coverage of effectiveness—of the ATO in managing the overall compliance risk and Treasury in meeting the policy intent for foreign investment in residential real estate.

Supporting findings

National residential land register

13. The ATO has been compiling a land register of residential real estate by tracking settlements that have occurred since 1 July 2016, and intends to populate the register by December 2018 and report thereafter. The register will use property data from state and territory land titles offices that contains foreign investment identifiers such as foreign investment application number and passport number. In light of the time required for the states and territories to pass legislation to enable the provision of property transaction data with foreign investment identifiers, the ATO has

developed interim arrangements to populate the register using data obtained through self-registration processes by foreign investors who have purchased residential real estate.

14. The ANAO's analysis identified serious deficiencies in populating the register with reliable data. There is likely under-reporting of self-registrations², over-reporting of foreign identity information in state property data³ and low levels of matching between datasets for foreign investment applications, self-registrations of foreign investment in residential property and state property data.⁴ Consequently, the ATO will need to undertake extensive manual verification processes in coming years to enable the register to provide accurate information about the nature and extent of foreign investment in residential real estate and produce reliable intelligence for compliance purposes.

Compliance strategies and voluntary compliance

15. The ATO does not have a compliance and enforcement strategy but has a reasonable basis for developing such a strategy, as it has undertaken a risk assessment of foreign investment in residential real estate and identified corresponding risk treatments. In preparing a compliance and enforcement strategy, the ATO should analyse compliance outcomes to inform targeted compliance approaches, address weaknesses in existing controls and incorporate measures of control effectiveness.

16. The ATO's information about foreign investment in residential real estate is comprehensive and readily accessible to foreign investors, stakeholders and the general public through the websites of the ATO and the Foreign Investment Review Board, which include information products in one language other than English (Chinese). There is also a residential foreign investment real estate help line and email inbox, avenues for community and stakeholder engagement, and use of social media. Activities are managed through an up-to-date communication strategy. There would be benefit in the ATO undertaking a broad evaluation of the residential foreign investment communication program to inform future communication strategies.

Detection and investigation

17. The ATO has partially effective processes to detect non-compliance with foreign investment obligations for residential real estate. It detected some 4300 cases of potential non-compliance from mid-2015 when it gained responsibility for compliance through January 2018, mainly from community or self referrals or through approval processes for foreign investors. While the ATO has

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- 2 While there were a number of self-registrations that could be used to populate the register (2653 to mid-December 2017), there may have been significant levels of non-registration, as the registrations represented only 7.1 per cent of applicants for such foreign investments from 1 July 2015 to mid-December 2017.
 - 3 New South Wales (NSW) was the only jurisdiction that had data available with foreign identifiers. The ANAO's analysis identified 23 431 properties in the NSW data with at least one potential foreign identifier, which was almost twice as high as the number of foreign investors who applied for residential real estate in NSW in 1 July 2015 to 13 December 2017 (12 278). The difference is likely to reflect reporting of information in the foreign identifier fields by non-foreign investors (particularly for the nationality or citizenship and passport number fields).
 - 4 Of 504 self-registrations of foreign investment in residential real estate in NSW in 1 July 2016 to 17 December 2017, there were only 56 exact matches with data from application approvals and from NSW property transaction records.

established a data matching program to actively detect non-compliance, as at April 2018 the program had not addressed all identified key compliance risks and more work was required to mature its processes for actively detecting non-compliance.

18. The ATO has developed and implemented a largely effective program to address identified cases of potential non-compliance with foreign investment obligations for residential real estate in a limited timeframe. Since gaining compliance responsibilities from Treasury in May 2015 through January 2018, the ATO completed 3940 investigations that identified 1158 breaches and resulted in 1067 financial penalties totalling some \$5.5 million, and the disposal of 231 foreign-owned properties valued at \$284.9 million.⁵ The key challenge for the ATO going forward will be addressing the more serious instances of non-compliance with the foreign investment framework; namely, demonstrating wilful non-compliance with obligations and applying criminal and civil penalties. There is also scope for the ATO to improve processes for escalating cases for investigation.

Monitoring and reporting

19. The ATO has over 20 indicators of success for its compliance activities for foreign investment in residential real estate, which it has measured for inclusion in a variety of internal communication and compliance processes. However, the ATO has not yet used the results to broadly assess its effectiveness in managing the overall compliance risk that ‘failure of foreign persons to comply with residential real estate foreign investment rules will undermine the integrity of the foreign investment framework and community confidence’. Similarly, Treasury has not measured effectiveness in achieving the stated policy intent of encouraging foreign investment in new residential dwellings.

20. The ATO and Treasury have largely effective arrangements in place to report on compliance activities for foreign investment in residential real estate, which could be strengthened by more broadly reporting on the effectiveness of those activities. The ATO has extensive internal reporting on compliance activities for foreign investment in residential real estate and shares this information with Treasury. Consequently, the extent of coverage in the Foreign Investment Review Board’s annual reports and Regulator Performance Framework reports has expanded since 2014–15, and includes information on compliance investigations, outcomes and penalties imposed.

5 Treasury had undertaken very little compliance activity prior to the ATO gaining responsibility for managing compliance with foreign investment obligations for residential property. For example, in the *Foreign Investment Review Board Annual Report 2014–15*, Treasury reported one forced disposal and no penalty information.

Recommendations

Recommendation no. 1
Paragraph 3.13 The Australian Taxation Office compiles and implements a residential foreign investment compliance and enforcement strategy, which draws on existing risk assessment and treatment documentation and information about the results of prior compliance activities.

Australian Taxation Office's response: *Agreed.*

Recommendation no. 2
Paragraph 4.13 The Australian Taxation Office prioritises developing and finalising data matching rules to address key compliance risks to foreign investment in residential real estate.

Australian Taxation Office's response: *Agreed.*

Summary of entity responses

21. A summary of entity responses is shown below, with full responses at Appendix 1.

Australian Taxation Office

The ATO appreciates the ANAO's efforts to undertake this audit and to provide the feedback and suggestions contained within this report. The ATO considers this report to be supportive of our overall approach to managing the administration of the *Foreign Acquisitions and Takeovers Act 1975* and the Government's foreign investment policy for the foreign investor segment. The review recognises the efforts the ATO has made in a relatively short period of time to establish a new program of work for administering foreign investment obligations in respect of residential real estate.

In finding the ATO's program to address identified non-compliance as largely effective, the review has identified a number of areas that the ATO could focus on to further enhance its effectiveness, particularly with regards to detection of non-compliance. The review also acknowledges the processes that the ATO has implemented to overcome some of the challenges that it faces in compiling a land register of residential real estate.

The ATO agrees with the two recommendations contained in the report.

Department of the Treasury

The Treasury welcomes the overall conclusions and findings of the audit.

While the report does not contain any recommendations for the Treasury, we will consider the key learnings within the report in the context of the Treasury's role in relation to administering the foreign investment framework, including our overarching policy responsibilities.

Key learnings for all Australian Government entities

22. Below is a summary of key learnings identified in this audit report that may be considered by other government entities when implementing a compliance function.

Performance and impact measurement

- In monitoring the effectiveness of the implementation of policy (such as foreign investment in residential real estate), entities should monitor the effectiveness of both compliance activities and the achievement of the broader policy intent (in this instance channelling foreign investment into new dwellings).
- If relying on third-party data (such as the ATO relying on state and territory property transaction data to identify foreign investment in residential real estate) be conservative about timelines for implementation and careful about how to ensure the data is accurate.

Governance

- When decisions are being taken about where to place a function, consideration should be given to the expertise and capability of potential delivery entities and which entity has the best fit of skills to administer the function. In the case of managing compliance with foreign investment in residential real estate, the function would have been best placed initially into the ATO rather than Treasury.
- In commencing the administration of a new function, conducting a prospective risk assessment and risk treatment plan (as the ATO did at the outset of its management of compliance with foreign investment in residential real estate) provides a sound basis for establishing a risk-based compliance function and developing an effective compliance strategy.

Audit findings

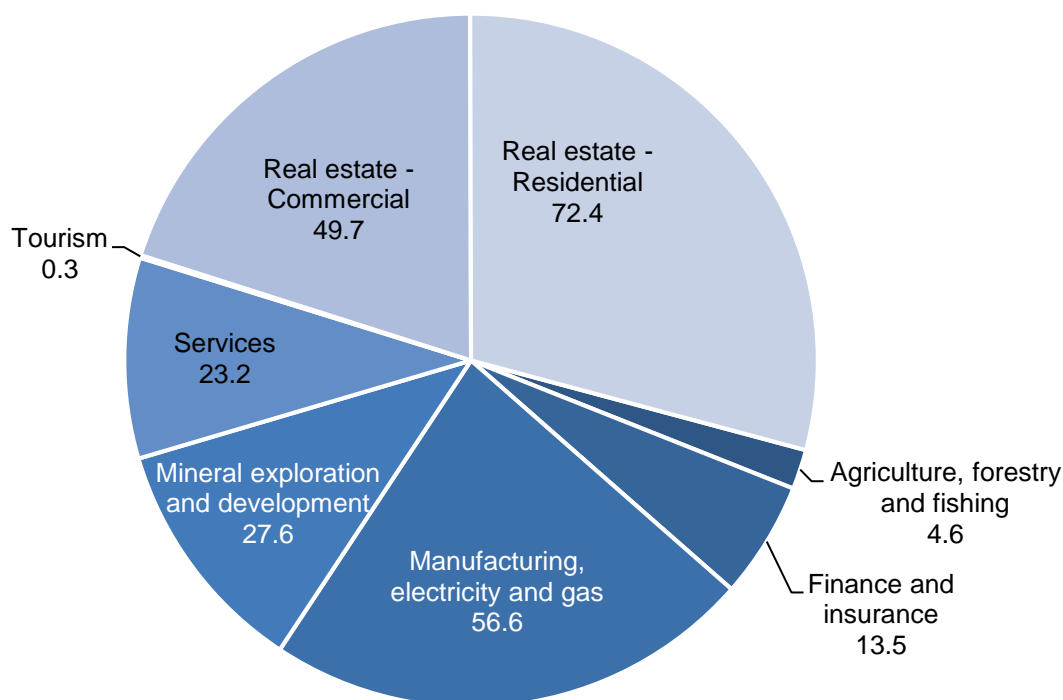
1. Background

Introduction

1.1 The Australian Government's policy is to welcome foreign investment, noting that foreign investment 'has helped build Australia's economy and will enhance the wellbeing of Australians by supporting economic growth and innovation into the future.'⁶ Foreign investment proposals are subject to the foreign investment framework and reviewed by the Australian Government on a case-by-case basis. The intention of the framework is to maximise investment flows, while protecting Australia's national interests. Factors that can be considered when assessing the impact of foreign investment on national interests include national security, the effect on competition, Australian tax revenues, resource use and stock production.

1.2 Foreign investment occurs across a range of markets, including business and land acquisitions (agricultural, mining and commercial), and residential real estate. Figure 1.1 illustrates the total value of foreign investment approvals (\$247.9 billion) by sector in 2015–16.

Figure 1.1: Value of foreign investment approvals by sector, 2015–16 (\$ billion)



Source: ANAO analysis of Foreign Investment Review Board information.

6 Treasurer, Australia's Foreign Investment Policy, p. 1, available from <http://firb.gov.au/files/2015/09/Australias_Foreign_Investment_Policy_December_2015_v2.pdf>, [accessed 2 May 2018].

The foreign investment framework

1.3 Australia's foreign investment framework primarily consists of the *Foreign Acquisitions and Takeovers Act 1975* and Australia's Foreign Investment Policy, which guide the Australian Government's decision making process when considering foreign investment proposals.

1.4 The Department of the Treasury (Treasury) is responsible for the foreign investment framework and the Treasurer reviews foreign investment proposals on a case-by-case basis to ensure they are not contrary to Australia's national interest. The Treasurer can make an order to prohibit a proposed foreign investment that is contrary to the national interest, or impose conditions on an investment on national interest grounds.⁷

1.5 Prior to 2015, Treasury was also responsible for compliance activities and assessing foreign investment applications. In the 2015–16 Budget, the Government announced a package of measures aimed at strengthening Australia's foreign investment framework. The package was introduced in response to a Senate committee inquiry report in 2013, *Foreign Investment and the National Interest*, which included 29 recommendations.

1.6 Additionally, the House of Representatives committee *Report on Foreign Investment in Residential Real Estate* in 2014 included 12 recommendations. In response to the second recommendation⁸ of the 2014 report, Treasury delegated responsibility for residential real estate under the foreign investment framework to the Australian Taxation Office (ATO), including the collection of fees, assessing applications, compliance and enforcement. Treasury retained responsibility for commercial real estate matters and other framework-wide administrative functions, such as external reporting.

1.7 The current foreign investment regime came into effect on 1 December 2015 and introduced the following features:

- stricter and more flexible penalties;
- an application fee regime;
- tighter rules relating to certain sectors (such as agriculture and critical infrastructure);
- an exemption certificate scheme for certain investments;
- a more stringent approach to foreign government investors; and
- creation of a register of foreign held interests in agricultural land and water.

1.8 Additionally, a register for foreign residential investment was established on 1 July 2016 and is expected to provide annual statistical reporting. Unlike the register for foreign investment in water and agriculture, there is no legislative requirement for the residential property register.

7 The Treasurer is supported by the Foreign Investment Review Board, which examines foreign investment proposals and advises on national interest implications.

8 Recommendation 2 from the *Report on Foreign Investment in Residential Real Estate* by the House of Representatives Standing Committee on Economics in November 2014 was 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.

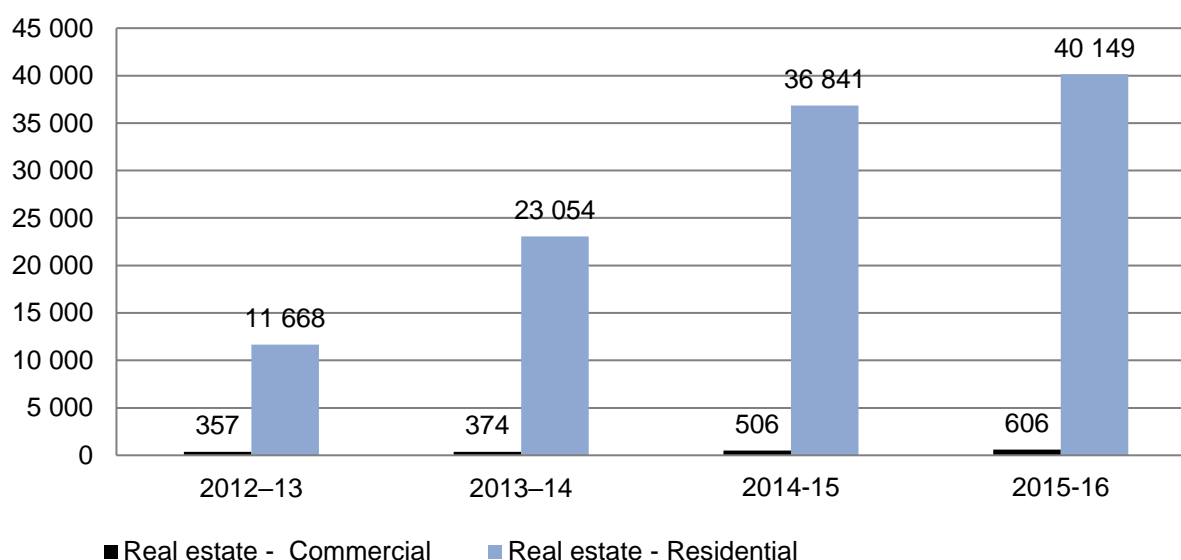
1.9 These changes to the foreign investment regime represented a new function within the ATO that required appropriate systems and processes to be put in place. The ATO received \$47 million to implement its residential real estate program over four years from 2015–16. In 2015–16, the ATO’s total operating costs for the program were \$9.2 million.⁹

Residential real estate

1.10 The foreign investment framework aims to channel foreign investment into new dwellings.¹⁰ The Foreign Investment Review Board states that this can create additional jobs in the construction industry, help support economic growth, and increase government revenues in the form of stamp duties and other taxes.¹¹ The Australian Government’s Foreign Investment Policy states that foreign investment enhances the wellbeing of Australians by increasing production, employment and income.¹²

1.11 The number of applications for foreign investment in Australian real estate has been increasing over recent years, as outlined in Figure 1.2. The total value of foreign investment approvals for residential real estate in 2015–16 was \$72.4 billion (as shown in Figure 1.1).

Figure 1.2: Number of applications for foreign investment in residential and commercial real estate



Source: ANAO analysis of Foreign Investment Review Board information.

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- 9 The ATO also received a \$10 million capital payment for the development of IT systems to support the introduction of the new fee regime, the foreign ownership registers and the residential real estate application process, compliance and penalty programs.
- 10 There is no legislative requirement that foreign investors purchase only new dwellings. The requirement that non-resident foreign investors purchase only new dwellings arises from the foreign investment policy.
- 11 Foreign Investment Review Board, *Guidance Note 1*, p. 1, available from <<http://firb.gov.au/resources/guidance/gn01/>>, [accessed 2 May 2018].
- 12 Treasurer, Australia’s Foreign Investment Policy, p. 1, available from <http://firb.gov.au/files/2015/09/Australias_Foreign_Investment_Policy_December_2015_v2.pdf>, [accessed 2 May 2018].

1.12 Foreign investors are required to gain approval prior to acquiring an interest in Australian real estate¹³, and applications are considered in light of the overarching principle that the proposed investment should increase Australia's housing stock by creating at least one new additional dwelling.¹⁴ The ATO has administered a new application fee for residential property from 1 December 2015.

Applications and approvals

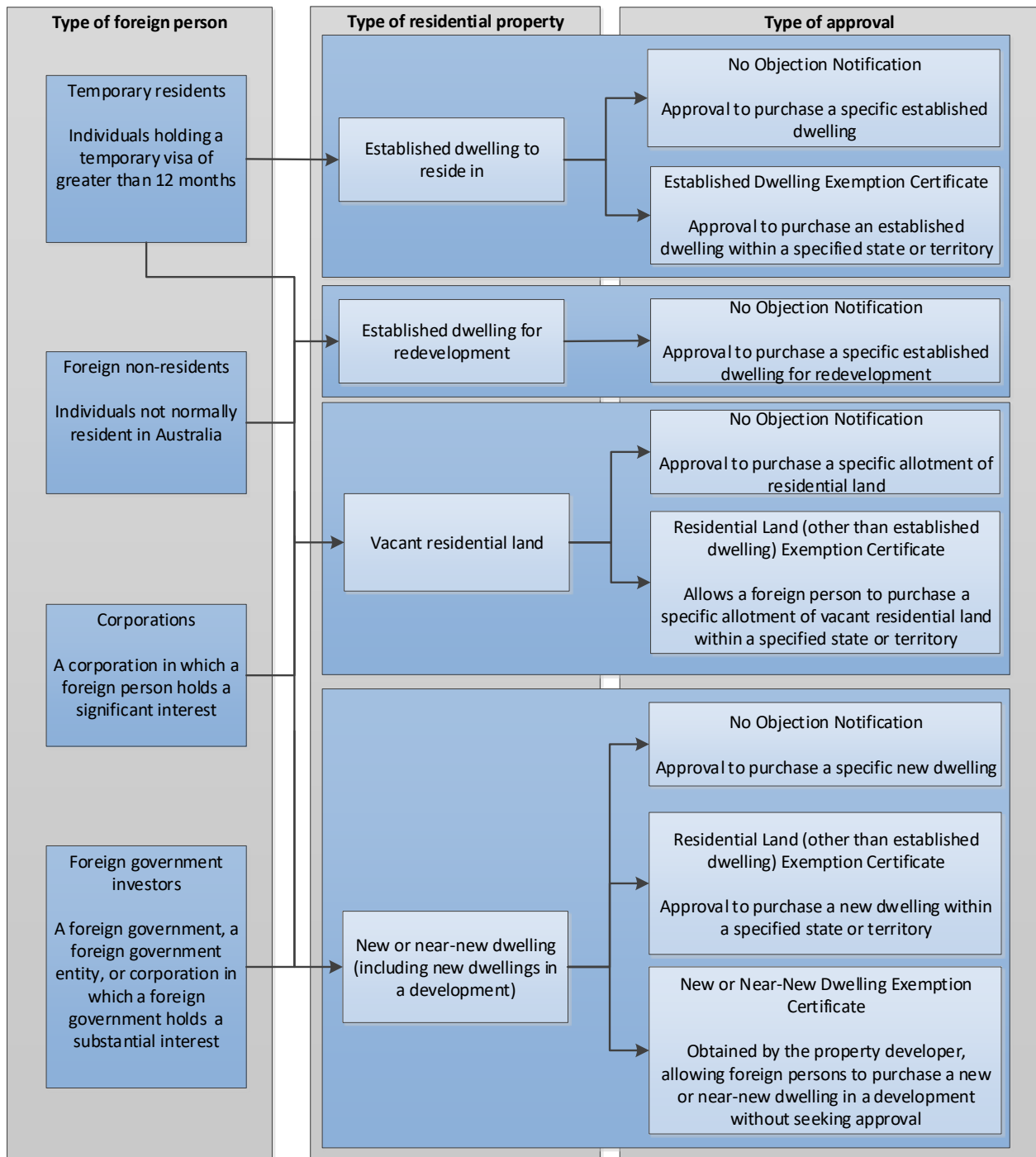
1.13 Foreign investors can apply to purchase specific residential properties, or can apply for an exemption certificate to allow them to purchase a certain class of property in a specified state or territory. The type of approval required is determined by the type of residential property. Approvals also contain conditions that must be satisfied, such as time periods in which actions must be taken. In addition to approval conditions, an annual vacancy charge for dwellings that are not rented out or occupied for more than six months per year applies from May 2017, with the first 12 month period to end May 2018.

1.14 The approval process and corresponding conditions for foreign investors in residential real estate are outlined in Figure 1.3.

13 Certain foreign persons are exempt from requiring approval to invest in Australian real estate. These are New Zealand citizens and holders of an Australian permanent resident visa.

14 Foreign Investment Review Board, *Guidance Note 1*, p. 1, available from <http://firb.gov.au/resources/guidance/gn01/>, [accessed 2 May 2018].

Figure 1.3: Types of residential real estate available to purchase by foreign persons and associated approvals



Source: ANAO analysis of ATO information.

Compliance and penalties

1.15 The ATO is responsible for detecting and investigating non-compliance with foreign investment obligations for residential real estate. Non-compliance behaviour can include purchasing property without approval and not complying with approval conditions. While the ATO promotes voluntary compliance with foreign investment obligations, a number of intelligence channels are in

place to assist it to detect non-compliance, including community referrals and referrals from other government departments. The ATO has also established a data matching program using data from other government departments and private sector entities to detect non-compliance.

1.16 Non-compliance with residential real estate obligations may result in the application of retrospective fees, penalties and infringement notices. The Treasurer can also require foreign investors to dispose of their interest in residential real estate in cases of non-compliance, by issuing a disposal order. As part of the reforms to the foreign investment framework, civil penalties were introduced and existing criminal penalties were strengthened.

Audit approach

1.17 The ANAO selected foreign investment in residential real estate for audit because of the extent of parliamentary and public interest in the issue, including concerns that foreign investors were not complying with foreign investment obligations and purchasing properties they were not entitled to own. The audit would also indicate the impact on compliance with foreign investment in residential real estate arising from the change in administrative arrangements.

1.18 The audit objective was to assess the effectiveness of the ATO's and Treasury's management of compliance with foreign investment obligations for residential real estate.

1.19 To form a conclusion against this objective, the ANAO adopted three high-level criteria:

- compliance and enforcement strategies and detection arrangements were in place to support compliance activities;
- activities were undertaken to promote voluntary compliance and effectively address identified instances of potential non-compliance; and
- the effectiveness of compliance arrangements was monitored and reported.

1.20 The audit did not examine the:

- implementation of legislative changes to the foreign investment framework in 2015;
- assessment of applications;
- implementation of the annual vacancy charge; and
- responsibility of Treasury to administer the foreign investment framework in relation to business, agricultural land and commercial land proposals.

Audit methodology

1.21 The audit methodology included reviewing internal ATO guidance, reporting, communication and evaluation plans, and interviewing key ATO and Treasury staff and stakeholders. The ANAO undertook data analysis of the application and self-registration data sets as well as state and territories land titles data. The ANAO did not receive any contributions from the public through its website in relation to this audit.

1.22 The audit was conducted in accordance with the ANAO Auditing Standards at a cost to the ANAO of approximately \$380 000.

1.23 Team members for this audit were Kylie Jackson, Renee Hall, Sonya Carter, Dung Chu, Fei Gao, Haydn Thurlow and Andrew Morris.

2. National residential land register

Areas examined

The ANAO examined the effectiveness of the ATO's processes for compiling a national residential land register.

Conclusion

The ATO has developed processes for compiling a land register of residential real estate but faces considerable challenges in populating the register with reliable data in coming years, which it needs to overcome in order to be effective.

Area for improvement

The ANAO made two suggestions aimed at the ATO taking steps to ensure the accuracy of foreign identifier data in state and territory real property transfers reports (paragraphs 2.15 and 2.25), and increase the number of registrations of foreign purchasers of residential real estate to support completeness of the register in the near term (paragraph 2.20).

Is the ATO effectively compiling a land register of residential real estate?

The ATO has been compiling a land register of residential real estate by tracking settlements that have occurred since 1 July 2016, and intends to populate the register by December 2018 and report thereafter. The register will use property data from state and territory land titles offices that contains foreign investment identifiers such as foreign investment application number and passport number. In light of the time taken by the states and territories to pass legislation to enable the provision of property transaction data with foreign investment identifiers, the ATO has developed interim arrangements to populate the register using data obtained through self-registration processes by foreign investors who have purchased residential real estate.

The ANAO's analysis identified serious deficiencies in populating the register with reliable data. There is likely under-reporting of self-registrations, over-reporting of foreign identity in state property data and low levels of matching between datasets for foreign investment applications, self-registrations of foreign investment in residential property and state property data. Consequently, the ATO will need to undertake extensive manual verification processes in coming years to enable the register to provide accurate information about the nature and extent of foreign investment in residential real estate and produce reliable intelligence for compliance purposes.

Background

2.1 As noted in Chapter 1, the Government agreed to a recommendation from a 2014 House of Representatives Standing Committee on Economics report that the ATO would establish a foreign ownership register, drawing from state and territory land title data collection processes.¹⁵

2.2 A key finding from the report was that there was no accurate or timely data that tracked foreign investment in residential real estate. Recommendation 8 was 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.¹⁶

2.3 The Government indicated that working with data from the states and territories would avoid duplication and reduce regulatory costs for purchasers of property. The Government's response outlined that the intent of the register would be to provide essential information to better understand foreign investment trends and to aid in the detection of non-compliance with the foreign investment rules.

2.4 The national land register of foreign ownership consists of three components—agricultural land, water access entitlements and residential real estate. The registration of agricultural land and water access entitlements is required under legislation.¹⁷ To meet this requirement, the ATO established an online self-registration channel and completed a stocktake of foreign-owned agricultural property.¹⁸

2.5 There is no legislation underpinning the development of the residential land register. The ATO leveraged off the agricultural self-registration channel to require foreign investors to also register residential real estate acquisitions from 1 July 2016.

2.6 There will be no stocktake of foreign-owned residential real estate for the register. The volume of historical real property transactions was considered too time consuming and costly to capture.¹⁹ As indicated in paragraph 2.3, the intent was to rely on data from the states and territories, which is provided to the ATO for various purposes (including capital gains tax) to compile the residential land register. However, the states and territories were not collecting information necessary to develop the register, such as purchasers' nationality and other foreign identifiers. Instead, a requirement for foreign investors to register details of a successful acquisition 30 days after settlement was introduced for approvals after 1 July 2016. This requirement was enforceable as a formal condition of approval for approvals after 1 July 2017.

15 Standing Committee on Economics, Australian Parliament, *Report on Foreign Investment in Residential Real Estate* (2014).

16 Standing Committee on Economics, Australian Parliament, *Report on Foreign Investment in Residential Real Estate* (2014), p. xviii.

17 The agricultural register was established under the *Register of Foreign Ownership of Agricultural Land Act 2015*, and amendments passed on 1 December 2016 to establish the water entitlements register. The Commissioner of Taxation is required to report to the Treasurer on the operation of the *Register of Foreign Ownership of Agricultural Land Act 2015*, and also publish aggregate statistics.

18 The ATO released its first report of foreign investment in agricultural land holdings for 2015–16 in September 2016, and the report for 2016–17 in September 2017.

19 Treasury expects that reporting on the flow of residential land would, over time, provide a meaningful stock of foreign ownership data without the need for a large and costly stocktake.

Third-party data sharing arrangements

2.7 In 2013–14, the Australian Government announced a measure for the ATO to expand third-party data matching and reporting arrangements, which was deferred for one year in the 2014–15 Budget.²⁰ The measure was intended to introduce a legislated reporting regime for the provision of real property data from the states and territories to replace the ‘inadequate approach’ of acquiring data using the ATO’s general powers of acquisition.²¹ Accordingly, there was a need to amend taxation legislation to provide the basis for the legislated reporting regime.

2.8 The measure was also expected to improve the integrity, and increase the quantity, of data reported by the states and territories to the ATO. The extended information reporting requirements were intended to: expand the data matching capability with third-party reporter information; improve integrity of the foreign resident capital gains tax regime; improve compliance for capital gains tax, goods and services tax and other taxable events; and support data sharing between government entities.

2.9 The revised data collection and reporting arrangements expanded the data provided by the states and territories to include information about the foreign identity of property purchasers and vendors, and was therefore expected to also support the compilation of the residential land register. The states and territories agreed to revise their respective legislation as they were otherwise unable to collect the additional data provided for under the new reporting arrangements, such as property vendor identity data or foreign entity data.²²

2.10 While the Commonwealth legislative changes to support the revised reporting arrangements were implemented by 1 July 2016, most states and territories had not passed associated legislative changes by that time. Consequently, the revised reporting arrangements were not implemented from 1 July 2016, with the exception of New South Wales that was able to revise its legislation in time. Table 2.1 outlines the timing of the legislative changes and the number of real property transfer reports received by the ATO since 1 July 2016.

20 In the 2014–15 Budget, the implementation date for the third-party reporting and data matching elements of the measure was deferred from 1 July 2015 to 1 July 2016.

21 The *Taxation Administration Act 1953* was amended in November 2015, and consequently the states and territories were required to provide quarterly real property transfers reports to the ATO from 1 July 2016.

22 The revised reporting arrangements included the collection and storage of information that previously had not been required. Consequently, the states and territories needed to update their existing systems to accommodate these changes. Through a funding instrument (*Project Agreement for a National Register of Foreign Ownership of Land Titles*), the Australian Government provided \$16.0 million to the states and Australian Capital Territory for system upgrades. The Northern Territory did not agree to participate in the project agreement to update its information collection and storage systems.

Table 2.1: Status of states and territories land holdings data sharing arrangements

| Jurisdiction | Date legislation passed allowing collection and reporting of foreign identity data | First quarterly collection of foreign identity data | Number of quarterly reports received by March 2018 |
|------------------------------|--|---|---|
| New South Wales | 28 June 2016 | 1 July 2016 | 6 quarters reported |
| Tasmania | 8 May 2017 | 1 July 2017 | 2 quarters reported |
| Australian Capital Territory | 9 June 2017 | 1 July 2017 | 2 quarters reported |
| Victoria | 22 June 2017 | 1 July 2017 | 2 quarters reported |
| Queensland | 30 June 2017 | 1 Sept 2017 | 2 quarters reported |
| Western Australia | Legislation not passed | <ul style="list-style-type: none"> System for collecting foreign identity data released in September 2017 Some clients voluntarily provide foreign identity data | 1 quarter reported with some voluntarily provided foreign identity data |
| South Australia | Legislation not passed | <ul style="list-style-type: none"> System upgraded requiring transfer information to be completed electronically from September 2017 Some clients voluntarily provide foreign identity data | 1 quarter reported with some voluntarily provided foreign identity data |
| Northern Territory | 23 June 2017 ^a | <ul style="list-style-type: none"> Currently reporting in the old format^b Reporting using the legislated report (minus foreign identity data) expected in the first quarter of 2018–19 | Nil |

Note a: The legislation passed in the Northern Territory enables collection and reporting of all information not previously collected, except for the foreign identity data.

Note b: All jurisdictions except Northern Territory commenced property data reporting from 1 July 2016 using the legislated Real Property Transfers Report. Only New South Wales reported foreign identity data during 2016–17.

Source: ANAO analysis.

2.11 As illustrated in Table 2.1, as at February 2018 all states and the Australian Capital Territory were in a position to provide the expanded real property transfers reports.²³ Real property transfers reports include the following information:

- property details, including land title information, property address and other descriptors;
- transactional information, including transfer price, contract date and settlement date;
- identity data of the purchaser/transferee and vendor/transferor, including:

23 The Northern Territory is engaging with the ATO regarding its reporting and intends to provide most fields required for the national land register except for the foreign identifiers and some entity details.

- name, address and date of birth for individuals;
- name, address and Australian Business Number for non-individuals; and
- foreign identity details.²⁴

2.12 Real property transfers reports include mandatory, optional and conditional fields. Optional fields must be completed by the intermediary²⁵/reporting party if the data is available, and conditional fields become mandatory when the condition is met.

Accuracy of foreign identifier data in real property transfers reports

2.13 As shown in Table 2.2, foreign identifier information in the real property transfers reports are all optional fields.²⁶ This may result in lower completion of fields²⁷, but needs to be balanced with the time and cost involved across all property purchases in completing property transfer reports. Table 2.2 also shows the number of foreign identifier fields that had been completed in the New South Wales (NSW) property data from 1 July 2016 to 30 September 2017. NSW was the only jurisdiction that had collected foreign identifier data for that period.

Table 2.2: Reporting fields in New South Wales property data for foreign investment

| Reporting data field | Reporting requirement | Number of completed fields in NSW property data |
|-------------------------------------|-----------------------|---|
| Application number | Optional | 888 |
| Overseas entity registration number | Optional | 74 |
| Overseas entity identifier | Optional | 547 |
| Nationality or citizenship | Optional | 29 183 ^a |
| Passport number | Optional | 16 455 ^a |
| Visa number | Optional | 9 220 ^a |

Note a: There can be multiple owners for each property transaction, and permanent residents (exempt from gaining foreign investment approval) may declare nationality other than Australian, as well as provide passport and visa details.

Source: ANAO analysis of ATO data.

24 Foreign identity details can include foreign investment application number, overseas entity identifier, nationality or citizenship, passport number and visa details (refer Table 2.2).

25 Intermediaries include conveyancers and solicitors acting on behalf of clients in property transactions.

26 The ATO advised that it was not considered feasible to make the Foreign Investment Review Board (FIRB) application number or other foreign identity fields (such as passport and visa number) mandatory in the approved form for reporting of real property transfers by the states and territories. A primary reason was that it was not the intention of the law to delay settlement of a property transaction due to nationality or other foreign identifier information not provided by a client, particularly as only a small percentage of property transfers in Australia involve a foreign purchaser.

27 The ATO advised that it expects that the foreign identity fields (including application numbers and passport numbers) will be collected by the states and territories for a significant proportion of the foreign investment population. The ATO is dependent on intermediaries (conveyancers, lawyers, solicitors) obtaining the information from foreign persons and entering it into the relevant database for the states and territories to collect.

2.14 The ANAO's analysis identified 23 431 properties in the NSW data with at least one potential foreign identifier. This number is almost twice as high as the number of foreign investors who applied for residential real estate in NSW from 1 July 2015 to 13 December 2017 (12 278 as shown in Figure 2.2). The difference may reflect reporting of information in the foreign identifier fields by non-foreign investors (particularly for the nationality or citizenship and passport number fields). It may also reflect instances where foreign investors had purchased residential real estate without applying to do so.

2.15 The ANAO suggests that the ATO closely examines the accuracy of foreign identifier data in state and territory real property transfers reports and takes steps to make it more immediately useable for the purposes of the register of residential real estate. This may require substantial liaison with state and territory land titles offices to improve the accuracy of the foreign identifier data, including to ensure that it only includes foreign investors, and increased communication with intermediaries.

Self-registration of foreign ownership of residential real estate

2.16 The ATO advised that it had been relying on the information collected through the self-registration process as an interim measure until the states and territories were able to collect and report the complete new property data including foreign identifiers. The ATO further advised that the foreign identifier in the data from the states and territories is intended to match an existing FIRB application and should streamline the process of compiling the register.

2.17 Foreign investors submit information regarding their acquisitions through an online form on the ATO's website. The online registration form was originally developed to register information on agricultural land holdings and the ATO designed the form to also collect residential real estate registrations from 1 July 2016.

2.18 The registration form provided on the ATO website has a range of information fields relating to: application information; contact details; ownership interest details; and land details. Of the 81 fields presented online, 36 were mandatory and 25 were conditional fields.

Extent of self-registration

2.19 The ANAO examined the extent of self-registration by comparing the number of self-registrations from 1 July 2016 to 17 December 2017 with the number of approvals for foreign investments in residential real estate from 1 July 2015 to 13 December 2017, shown in Table 2.3. The ANAO acknowledges uncertainty in this calculation relating to the selection of different time periods for approvals data (1 July 2015 to 13 December 2017) compared to self-registration data (1 July 2016 to 17 December 2017)²⁸, and because application approvals represent proposed investment and not all foreign investment approvals result in a purchase.

28 The ANAO selected a period beginning 12 months prior to the commencement of the self-registration data as this provides a conservative estimate of the timeframe for applicants to search for a property, complete the purchase process and then self-register after settlement.

Table 2.3: Proportion of the ATO's self-registrations of approvals for foreign investments in residential real estate

| Type of foreign investor | Number of application approvals ^a | Number of self-registrations ^b | Percentage of self-registrations of application approvals |
|--------------------------|--|---|---|
| Individual | 35 966 | 2 549 | 7.1 |
| Company | 848 | 76 | 9.0 |
| Trustee | 330 | 28 | 8.5 |
| Total | 37 144 | 2 653 | 7.1 |

Note a: From 1 July 2015 to 13 December 2017.

Note b: From 1 July 2016 to 17 December 2017.

Source: ANAO analysis of ATO data.

2.20 As shown in Table 2.3, self-registrations represented 7.1 per cent of all approvals over the period. While it is not known how many approvals have resulted in a purchase, and therefore what percentage would represent full registration, the 7.1 per cent recorded provides some basis for considering there may be significant non-registration by foreign investors in residential real estate.²⁹ Accordingly, there would be merit in the ATO assessing the potential extent of non-registration and taking steps to improve the level of registration through education and other means (which could include simplifying the registration form to reduce a potential deterrent to self-registration).

2.21 The ATO advised in May 2018 that it had implemented strategies to increase the rate of self-registration, including through email prompter campaigns and visits to intermediaries. The ATO also advised that to mitigate risks to the integrity of the land register from under self-registration, it had conducted a comprehensive manual data matching exercise to identify property transfers that relate to a foreign investment approval.

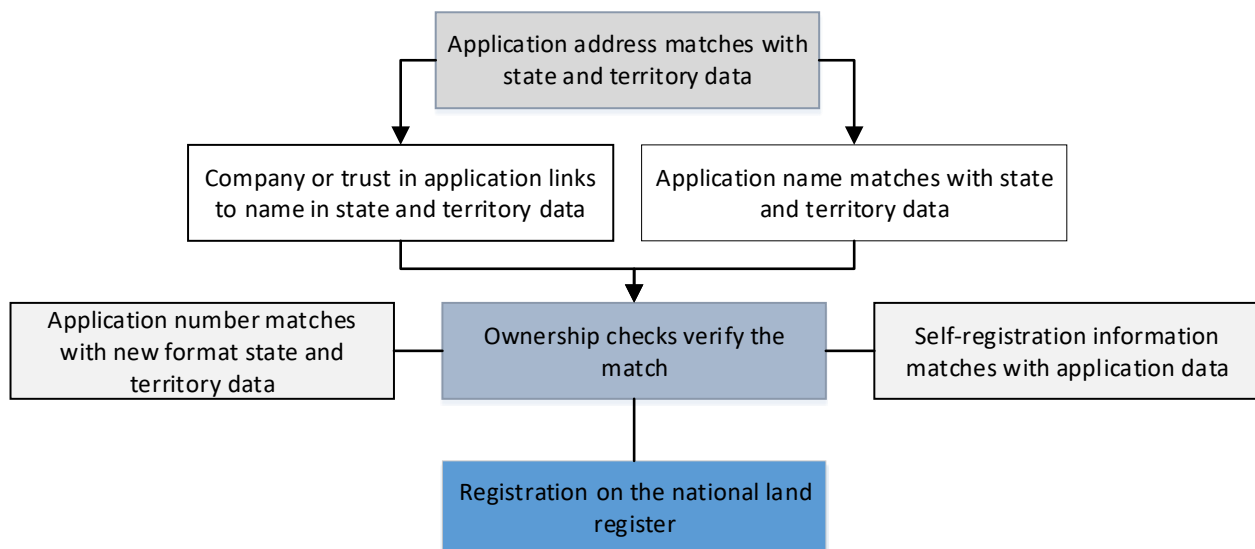
Compiling the national residential land register

2.22 As illustrated in Figure 2.1, to compile the residential land register the ATO matches state and territory land titles data to foreign investment application data, and manually verifies the information submitted through the self-registration process with:

- application data sets to confirm compliance with approval conditions; and
- states and territories data to confirm the residential real estate purchase details.³⁰

29 Considerable cost and time imposts are incurred in applying for approvals for foreign investment in residential real estate. Applicants would therefore presumably have strong intentions to purchase property and it would be surprising if only around 7.1 per cent of all approvals resulted in a purchase in the period examined.

30 The ATO uses self-registration data as the primary method to compile the residential land register, but is working to better match state and territory land titles data to foreign investment application data to reduce the reliance on self-registration in the future.

Figure 2.1: Residential land information compiled for the national land register

Source: ANAO analysis.

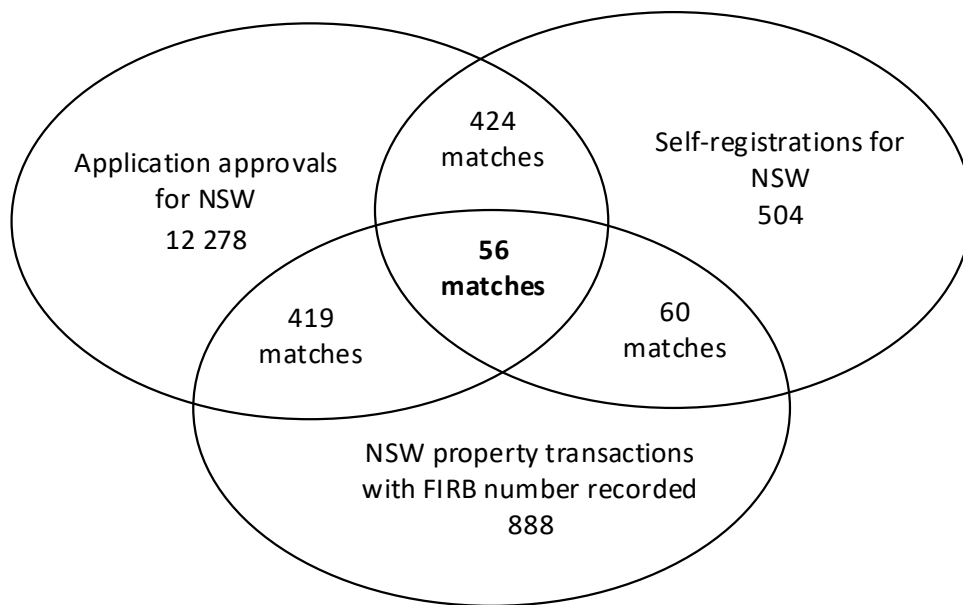
2.23 Of the 2653 self-registrations shown in Table 2.3, 2128 registrations (80.2 per cent) exactly matched the FIRB numbers in the application data, and 525 (19.8 per cent) did not have matched FIRB numbers.³¹ However, the extent of non-exact matches also highlights the need for considerable effort by the ATO to cleanse the data in compiling the register in coming years.

2.24 The ANAO extended the matching of FIRB numbers for self-registrations, foreign investment applications and NSW real property data only.³² This matching aimed to identify the number of foreign investors with approval who subsequently purchased a dwelling and also self-registered. The matching identified a small number and percentage of application numbers consistent across the three data sets, as illustrated in Figure 2.2.

31 There were 123 self-registrations containing FIRB application numbers in a non-valid format.

32 The ANAO tested application data from 1 July 2015 to 13 December 2017; NSW property transaction data from 1 July 2016 to 30 September 2017; and self-registrations from 1 July 2016 to 17 December 2017.

Figure 2.2: Data matching of potential foreign investor properties



Source: ANAO analysis of ATO information.

2.25 This analysis identified serious deficiencies in populating the register with reliable data, and further emphasises the importance of the ATO taking steps to improve the accuracy of data in real property transfers reports³³, and also in self-registrations.

2.26 The ANAO also matched information other than the application number between the FIRB application data and NSW real property data. As shown in Table 2.4, the ANAO developed degrees of confidence by matching the following information:

- name of purchaser;
- passport number;
- address of purchaser; and
- address of property purchased.

2.27 Table 2.4 indicates that the number of high and medium confidence matches for NSW (51 and 122 or 113 respectively) represented a small proportion of the number of self registrations and applications (504 and 12 278 respectively from Figure 2.2), and there was considerable variation in the three types of low confidence matches for NSW.

33 As shown in Figure 2.2, of 888 NSW property transactions with a FIRB application number recorded, there were only 419 matches (47 per cent) with the number in the application approvals.

Table 2.4: Potential matches of data from foreign investment applications with NSW real property data

| Data matches | Details | NSW |
|---------------------------|--|-------|
| High confidence matches | First name, middle name, family name, passport number, address of purchase and address of purchaser | 51 |
| Medium confidence matches | First name, middle name, family name, passport number and address of purchase | 122 |
| | First name, middle name, family name, address of purchase and address of purchaser | 113 |
| Low confidence matches | First name, middle name, family name and address of purchase | 339 |
| | First name, middle name, family name and address of purchaser | 747 |
| | First name, middle name, family name and passport number | 1 237 |

Source: ANAO analysis of ATO information.

2.28 In the context of the large number of properties purchased between 1 July 2016 and 30 September 2017 (427 946 properties for NSW), the ANAO's testing revealed considerable levels of non-matches that will require manual verification by the ATO.

2.29 The ATO intended to provide an interim report on the register of foreign investment in residential real estate to Treasury in March 2018, however the report is yet to be prepared. The ATO aims to populate the register by December 2018 and prepare yearly reporting on the register once the states' and territories' information is standardised from 2019 onwards.³⁴

34 The ATO will prepare the report and provide it to Government for publication.

3. Compliance strategies and voluntary compliance

Areas examined

The ANAO examined the ATO's compliance strategies and voluntary compliance activities aimed at addressing non-compliance with foreign investment obligations for residential real estate.

Conclusion

The ATO has assessed and addressed compliance risks in relation to foreign investment obligations for residential real estate but has not yet compiled and implemented a compliance and enforcement strategy. To promote voluntary compliance with those obligations, the ATO has developed a series of communication strategies. The strategies, which have largely been implemented, incorporate a multi-platform communication approach targeting key audiences with priority messages.

Areas for improvement

The ANAO made one recommendation aimed at the ATO developing a compliance and enforcement strategy in relation to residential foreign investment obligations (paragraph 3.13).

The ANAO made seven suggestions aimed at: improving the ATO's assessment of risk control effectiveness (paragraph 3.3); improving the alignment between risk documentation and communication plans (paragraph 3.18); publishing residential foreign investment information in additional foreign languages (paragraph 3.21); improving the usability, and clarifying the status, of guidance notes (paragraphs 3.24 and 3.25); considering additional prompter campaigns (paragraph 3.29); including targets and qualitative indicators in future communication strategy evaluation plans (paragraph 3.38); and undertaking a formal evaluation of the entire foreign investment communication program (paragraph 3.41).

Does the ATO have an effective compliance and enforcement strategy in place?

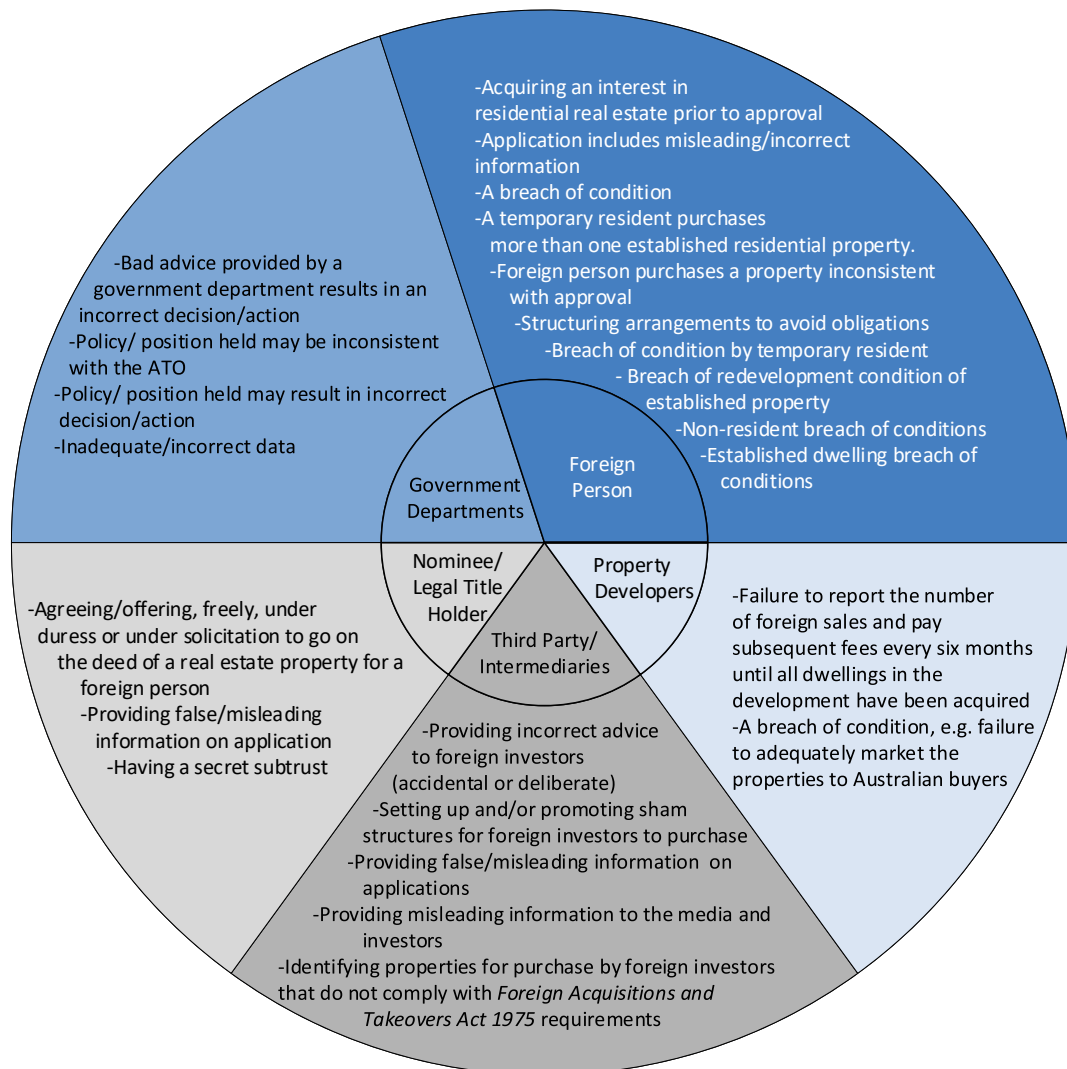
The ATO does not have a compliance and enforcement strategy but has a reasonable basis for developing such a strategy, as it has undertaken a risk assessment of foreign investment in residential real estate and identified corresponding risk treatments. In preparing a compliance and enforcement strategy, the ATO should analyse compliance outcomes to inform targeted compliance approaches, address weaknesses in existing controls and incorporate measures of control effectiveness.

3.1 The ATO does not have a compliance and enforcement strategy but has a documented risk assessment for foreign investment in residential real estate and a corresponding risk treatment plan (both completed in December 2016).

Risk assessment of foreign investment in residential real estate

3.2 The ATO's risk assessment of foreign investment in residential real estate outlines risk drivers³⁵, as well as cultural influences and individuals' psychological traits. It also identifies potential risk participants and the non-compliance risks associated with those participants, as outlined in Figure 3.1.

Figure 3.1: Potential non-compliance risks and participants for foreign investment in residential real estate



Source: ANAO analysis of ATO's risk assessment of foreign investment in residential real estate.

3.3 The risk assessment also outlines the controls in place to prevent, detect and mitigate risks associated with foreign investment in residential real estate. The assessment was of the expected effectiveness of those controls, as there was lack of evidence to determine actual effectiveness. On this basis, the ATO identified and assessed ten controls as being effective or partially effective, as

35 For example, a lack of awareness of compliance obligations among risk groups such as foreign investors and intermediaries.

shown in Table 3.1. No controls were assessed as being ineffective.³⁶ Going forward, the ATO's risk assessments should incorporate an assessment of the demonstrated effectiveness of controls, and in doing so could include some of the measures outlined in Table 3.1.

Table 3.1: The ATO's assessment of risk controls for foreign investment in residential real estate, and rating of effectiveness

| Control | Control type and ATO assessment | Reason for the ATO's assessment | The ANAO's suggestions of measures that could inform the ATO's assessment of the effectiveness of controls |
|--|-------------------------------------|---|--|
| Foreign investment real estate helpline | Preventative Partially effective | Help line does not accommodate international time differences and does not offer immediate translation services | <ul style="list-style-type: none"> No. of calls that are answered/not answered Client satisfaction with helpline experience Types of queries Clients' action following help line call |
| Foreign investment self-disclosure | Preventative Effective | Amnesty period was available for self-disclosure from May to November 2015 ^a | <ul style="list-style-type: none"> No. of people who self-disclosed compared with no. of people expected to self-disclose and estimated size of non-compliance pool Level of non-compliance among those who self-disclosed |
| Education and information | Preventative Effective | Activities undertaken to educate and inform stakeholders | <ul style="list-style-type: none"> No. of people attending events and/or visiting websites Feedback from stakeholders in relation to the relevance, timeliness and accuracy of information Reduction in the number of queries from stakeholders No. of people self-disclosing non-compliance |
| New penalty regime | Preventative Effective | New civil and increased criminal penalties should deter non-compliance | <ul style="list-style-type: none"> Level of awareness of penalties among risk participants Rate of application of penalties by the ATO Level of unsolicited media coverage resulting from the application of penalties Trend in compliance rates |
| Third party involvement in property transactions | Preventative Partially effective | Third parties provide control as most intermediaries will require evidence of approval from investors | <ul style="list-style-type: none"> Trend in compliance rates, including among intermediaries Level of awareness of responsibilities and penalties among intermediaries |

³⁶ The ATO defines effective controls as effective and reliable at managing the risk, and meeting or exceeding their intended purpose. Partially effective controls are those that provide some management of risk but are only partially meeting their intended purpose.

| Control | Control type and ATO assessment | Reason for the ATO's assessment | The ANAO's suggestions of measures that could inform the ATO's assessment of the effectiveness of controls |
|--------------------------------------|--|--|---|
| Legislative changes | Preventative/ Mitigative Effective | Changes to the <i>Foreign Acquisitions and Takeovers Act 1975</i> and the introduction of the <i>Foreign Acquisitions and Takeovers Fees Imposition Act 2015</i> | <ul style="list-style-type: none"> Trend in compliance rates, including the application of new and revised penalties Awareness of new and revised penalties among risk participants Rate of application of penalties |
| Reduced application processing times | Preventative/ Mitigative Effective | Investors will be unable to avoid foreign investment obligations due to time constraints in purchasing a property | <ul style="list-style-type: none"> No. of applications that are withdrawn or cancelled Trend in compliance rates |
| Community referral line | Detective Effective | Members of the public can report suspected non-compliance through the line that is easy to access and use | <ul style="list-style-type: none"> No. of referrals received via the line No. of referrals that result in confirmed non-compliance Awareness of the line among community members |
| Case selection (methods developed) | Detective Partially effective | Data matching is used to detect non-compliant behaviour | <ul style="list-style-type: none"> Proportion of data matching outcomes that result in confirmed non-compliance, including detection of serious non-compliance |
| Compliance activity | Detective Effective | Twenty-one per cent non-compliance rate confirmed among investigated cases (including residential, commercial and agriculture) | <ul style="list-style-type: none"> No. of cases identified No. of cases investigated Outcomes of cases investigated |

Note a: The amnesty period included reduced penalties for foreign investors who voluntarily disclosed breaches of the foreign investment framework. The amnesty period was from 2 May 2015 to 30 November 2015 and had concluded prior to the dates of the risk assessment and risk treatment plan (December 2016).

Source: ATO risk assessment of foreign investment in residential real estate and ANAO analysis.

3.4 The ATO's December 2016 risk assessment for foreign investment in residential real estate also identified four future controls, as shown in Table 3.2.

Table 3.2: Future controls for foreign investment in residential real estate, and status as at January 2018

| Future control | Type of control | Description of control | ATO's assessment of the status of controls as at January 2018 |
|---|-----------------|---|---|
| Case selection methods (under development) | Detective | Additional data matching rules (as outlined in Chapter 4) were being developed to identify different types of non-compliance for example, property purchases prior to approval. | Six data matching rules have been implemented; two are under development; and two are yet to be developed. ^a |
| Data systems, storage and collection | Mitigative | Recreating Treasury's historical database. ^b Profiling land owners. | Implemented. |
| Registration of foreign persons leaving Australia | Detective | Identifying temporary residents using Department of Home Affairs and residential investment register data. | Implemented. |
| Compliance work focusing on structures | Detective | Dedicating an ATO officer to examine structures implemented to avoid <i>Foreign Acquisitions and Takeovers Act 1975</i> obligations. | Implemented. |

Note a: Other information provided by the ATO indicated that of the 32 data matching rules, as at March 2018: 15 had been developed; eight were under development; six had not yet been started; two were considered redundant; and one remained under consideration (see Chapter 4).

Note b: The ATO advised that the database combines the foreign investment approvals completed by Treasury with the foreign investment approvals completed by the ATO.

Source: ATO risk assessment of foreign investment in residential real estate.

3.5 Overall, the ATO's risk assessment was that the preventative controls were partially effective, while detective and mitigative controls were effective. The risk assessment noted a gap in the coverage of mitigative controls to be addressed by the implementation of the future controls (which have subsequently largely been implemented).

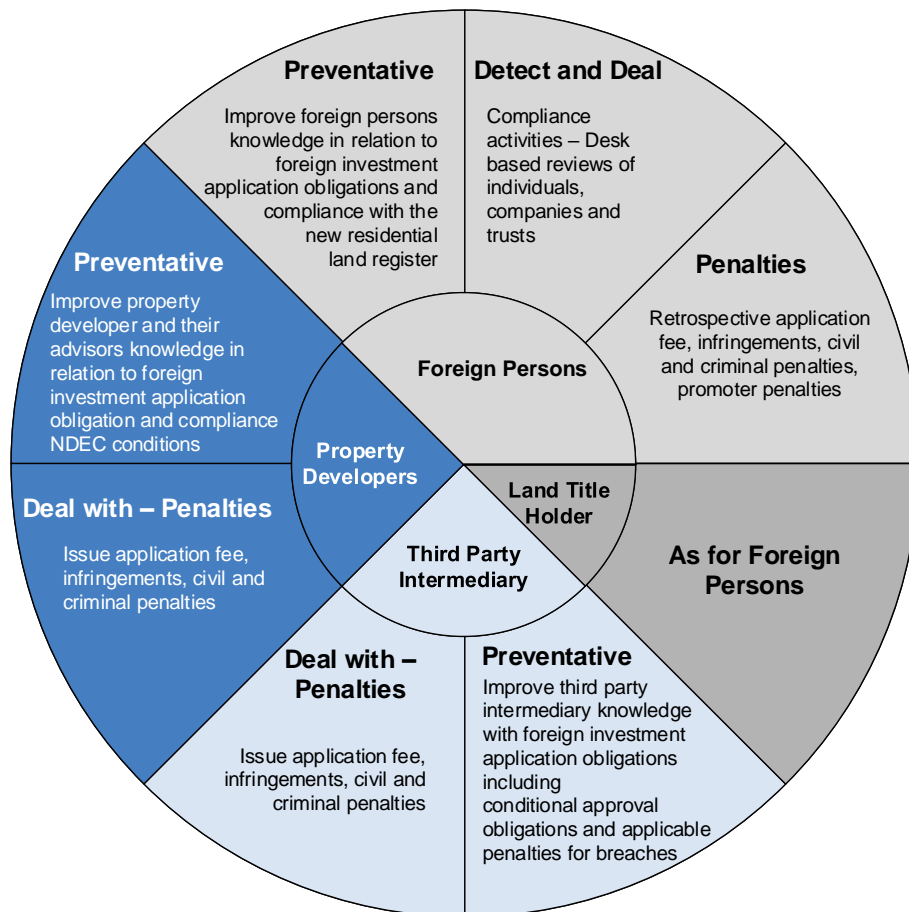
3.6 The ANAO considers that the ATO had overstated the effectiveness of the detective and mitigative controls as: detection activities had not addressed risks posed by intermediaries; and the ATO's data matching program was at an early stage in addressing key compliance risks (as discussed in Chapter 4).

3.7 Strengthening the ATO's risk assessment processes to be informed by evidence demonstrating the effectiveness of controls will provide greater confidence in the accuracy of assessments as well as assist to identify controls that need to be improved or introduced. The ATO advised the ANAO that while the assessment of effectiveness of controls was initially necessarily prospective in nature, subsequent risk assessments will incorporate evidence of the effectiveness of controls where practical.

Risk treatment plan

3.8 The risk treatment plan identifies treatments to address the non-compliance risks for foreign investment in residential real estate that were identified in the risk assessment, as illustrated in Figure 3.2.

Figure 3.2: High-level treatments to address compliance risks for foreign investment in residential real estate



Note: NDEC is New Dwelling Exemption Certificate.

Source: ATO risk treatment plan for foreign investment in residential real estate.

3.9 Some of these high-level treatments are supported by lower-level treatments. For example, improving the knowledge of investors and intermediaries is supported by targeting specific audiences through relevant communication channels. For 11 of the 14 lower-level treatments, responsibility is assigned to ATO officers for implementation in a project plan attached to the treatment plan.³⁷ As at April 2018, all treatments were being implemented, and had ‘ongoing’ listed as their due date.

Compliance and enforcement strategy

3.10 While the ATO has not compiled a compliance and enforcement strategy, the risk assessment and treatment plan provide a reasonable basis for developing one. The ATO advised the ANAO that it intends to update its risk assessment and treatment plans on an annual basis.

³⁷ Three of the treatments were not assigned to a responsible officer for implementation: mail out prompter campaign to foreign investors with vacant properties; prompter campaign to remind property developers with new dwelling exemption certificates of their obligations to reconcile and report on the subsequent sale of development; and real-time processes at application lodgement to issue infringements where properties were acquired prior to seeking approval.

Leveraging off this process, the ATO could prepare a compliance and enforcement strategy that reflects current compliance risks and intelligence, for example:

- analysing compliance outcomes to inform targeted compliance approaches including geographic areas to target or particular types of foreign investment (refer Chapter 4); and
- identifying key compliance messages to be communicated, such as legislative changes.

3.11 Developing a compliance and enforcement strategy that clearly links types of non-compliant behaviour with penalties and the ATO's detection and investigation activities would assist the ATO to prioritise its activities to encourage compliance with foreign investment obligations for residential real estate.

3.12 The ATO could also consider how to use elements of the strategy in activities to educate stakeholders of their obligations and the penalties for non-compliance. There is limited publicly available information about the ATO's residential foreign investment compliance and enforcement approach, and where information is available, it is disseminated in some of the 50 guidance notes published on the Foreign Investment Review Board's website.³⁸ Thirty-seven of these guidance notes are relevant to residential foreign investment, of which:

- thirty indicate that penalties may apply to breaches of Australia's foreign investment framework;
- one contains information in relation to an ATO investigation activity³⁹;
- eleven provide examples of non-compliant behaviour and the relevant penalties; and
- ten provide examples of non-compliant behaviour but do not identify the relevant penalties.

Recommendation no.1

3.13 The Australian Taxation Office compiles and implements a residential foreign investment compliance and enforcement strategy, which draws on existing risk assessment and treatment documentation and information about the results of prior compliance activities.

Australian Taxation Office's response: *Agreed.*

3.14 *In addition to processes already underway to review existing risk assessment and treatment documentation for foreign investment in residential real estate, the ATO will compile a single compliance and enforcement document. In doing so, the ATO will look to draw from existing strategy and reporting documentation.*

38 Foreign Investment Review Board, *Guidance Notes* [Internet], available from: <<http://firb.gov.au/resources/guidance/>> [accessed 23 January 2018].

39 Guidance Note 5, *Residential real estate – Australian corporations, trusts and use of other persons*, indicated that the Treasurer or his delegate can issue a tracing notice requiring further information from a person in relation to ownership of a dwelling. Foreign Investment Review Board, *Residential Real Estate – Australian Corporations, Trusts and Use of Other Persons* [Internet], available from: <<http://firb.gov.au/resources/guidance/gn05/>> [accessed 31 January 2018].

Are voluntary compliance activities effective and well-targeted?

The ATO's information about foreign investment in residential real estate is comprehensive and readily accessible to foreign investors, stakeholders and the general public through the websites of the ATO and the Foreign Investment Review Board, which include information products in one language other than English (Chinese). There is also a residential foreign investment real estate help line and email inbox, avenues for community and stakeholder engagement, and use of social media. Activities are managed through an up-to-date communication strategy. There would be benefit in the ATO undertaking a broad evaluation of the residential foreign investment communication program to inform future communication strategies.

Communication strategies

3.15 The ATO developed a communication strategy in relation to foreign investment in September 2015 for the 2015–16 year, and has prepared a revised strategy for each subsequent financial year. The strategies cover foreign investment in both agriculture and residential real estate. The strategies outline communication approaches to target foreign investors and intermediaries through various channels, including social media, face-to-face educational opportunities, specialist channels to reach diverse audiences, and a foreign investment specific help line and email inbox.⁴⁰ Key messages are revised to reflect communication priorities such as changes to legislation and foreign investors' obligations.⁴¹

3.16 The ATO's foreign investment communication strategies have matured over time, as demonstrated by the inclusion of improved implementation plans with status sections for recording progress, and evaluation plans that identify communication objectives (see paragraph 3.40). Over time, the number of communication activities has decreased, with 58 activities in the period July 2015 to July 2016, 13 activities in the period July 2016 to July 2017 and one activity from July 2017 to January 2018.

3.17 The 2017–18 communication strategy outlines a new program of communication activities, including articles and public relations activities, and social media posts, which focus on renewed messaging about the water register and the introduction of the vacancy charge. In its 2018–19 communication strategy, the ATO could consider increasing the number of communication activities (subject to the evaluation suggested in paragraph 3.41), as well as placing a greater

40 The ATO also developed a communication strategy to support the implementation of the vacancy charge (refer Chapter 1).

41 Key messages included in the 2015–16 communication plan were the: strengthening of foreign investment obligations; implementation of stricter penalties and reduced penalty period; and introduction of application fees for foreign investment in real estate. Key messages outlined in the 2016–17 communication plan included: the unlikelihood of a waiver or refund of fees for residential foreign investment obligations; the requirement for foreign investors to register purchases of residential real estate; and information about breaches and penalties. The key message outlined in the 2017–18 communication plan was the implementation of the vacancy charge.

emphasis on messages in relation to foreign investment obligations for residential real estate, including the residential land register⁴² to assist in improving data quality.

3.18 The communication strategies generally address compliance risks identified in the ATO's foreign investment in residential real estate risk assessment and treatment plan (see paragraphs 3.2 to 3.11). As illustrated in Table 3.3, some areas of misalignment that the ATO could consider addressing include identifying the: ATO and Foreign Investment Review Board (FIRB) websites in the risk assessment or treatment plans; and key agent program⁴³ in the communication strategy.

Table 3.3: Identification of communication activities in the ATO's foreign investment in residential real estate risk assessment and risk treatment plans

| | Risk assessment – controls | Risk treatment plan – treatments |
|---|----------------------------|----------------------------------|
| In communication strategies | | |
| Social media | Yes | No |
| ATO webpages | No | No ^a |
| Foreign Investment Review Board website | No | No |
| Foreign Investment Review Board helpline | Yes | No |
| Foreign Investment Review Board mailbox | No | Yes |
| Foreign Investment Reforms Working Group | No ^b | Yes |
| Established ATO channels (business bulletins, tax professional newsroom and small business newsroom) | No | Yes |
| Face-to-face educational activities (including seminars and information booths) | Yes | Yes |
| Media articles and public relations | No | Yes |
| Communication via community/specific audience channels (e.g. Chinese community TV and Multicultural NSW mailing list) | Yes | Yes |
| Prompter campaigns | No | Yes |
| Not in communication strategies | | |
| Key agent program | Yes | Yes |

Note a: Activity mentioned as a data source, not a treatment.

Note b: Activity mentioned in the risk event, not as a control.

Source: ANAO analysis of ATO communication strategies, risk assessment and treatment plans for foreign investment in residential real estate.

42 In early 2018, the ATO commenced communication activities to improve the rate of self-registration on the land register including email prompter campaigns and visits to intermediaries.

43 The ATO's key agent program targets high consequence tax professionals for consultation to assist with identification and resolution of issues within the tax system. The program is identified in the risk assessment and treatment plans for foreign investors in residential real estate.

3.19 The activities outlined in the 2015–16 and 2016–17 communication strategies have been implemented, except for the prompter campaigns that were partly implemented (see paragraphs 3.28 to 3.29). The 2017–18 communication strategy was being implemented at the time of audit fieldwork.

Online guidance

The ATO's website

3.20 The ATO's website has webpages to inform foreign investors of their obligations under the *Foreign Acquisitions and Takeovers Act 1975*, including a page specifically relating to residential foreign investment.⁴⁴ These pages include information on foreign investors' obligations before and after investment as well as in relation to breaches and changes of circumstances.

3.21 The ATO's webpages in relation to foreign investors are readily accessible, and though containing limited detail, link to the more comprehensive information available on the Foreign Investment Review Board's website. The ATO's website also includes links to fact sheets in traditional and simplified Chinese (as investors from Chinese speaking countries comprise 65 per cent of residential foreign investment applications and 54 per cent of breaches). There is an opportunity to publish material in other languages for the benefit of investors who reflect a significant proportion of the foreign investment application population. For example, as at January 2018, six per cent of breaches were committed by Malaysian investors and three per cent of breaches were committed by Indonesian investors.

3.22 The ATO's website also includes webpages dedicated to legislative, corporate and administrative tax news. These webpages were used to distribute information during 2015 and early 2016 on the foreign investment obligations, and are primarily aimed at educating intermediaries.⁴⁵ The ATO has not used these webpages to distribute foreign investment information since early 2016. The ATO should consider using these webpages to disseminate new information such as changes to legislation, particularly as they focus on targeting intermediaries and are the primary way of addressing the risk of intermediaries assisting in breaches according to the ATO's risk treatment plan for foreign investment in residential real estate.

Foreign Investment Review Board (FIRB) website hosted by Treasury

3.23 Most information about residential foreign investment obligations is available on the Foreign Investment Review Board website.⁴⁶ The guidance notes available on the website provide

44 Australian Taxation Office, Residential investment, [Internet], ATO, available from <<https://www.ato.gov.au/General/Foreign-investment-in-Australia/Residential-investment/>> [accessed 13 March 2018].

45 Australian Taxation Office, *Tax Professionals Newsroom*, ATO, Available from <<https://www.ato.gov.au/Tax-professionals/Newsroom/>> [accessed 13 March 2018].

Australian Taxation Office, *Business Bulletins*, ATO, available from <https://www.ato.gov.au/business/large-business/in-detail/business-bulletins/?page=1#Business_bulletin_articles> [accessed 13 March 2018].

Australian Taxation Office, *Small Business Newsroom*, ATO, available from <<https://www.ato.gov.au/Newsroom/smallbusiness/>> [accessed 13 March 2018].

46 The Foreign Investment Review Board website was redesigned and relaunched in December 2015 to coincide with changes to the *Foreign Acquisitions and Takeovers Act 1975*, as detailed in Chapter 1. Available from <<http://firb.gov.au/real-estate/>> [accessed 13 March 2018].

a significant amount of information on a range of topics relevant to residential and other areas of foreign investment. For example, the guidance notes include information on the legislative obligations of foreign investors, application fees, penalties, definitions and exemptions.⁴⁷

3.24 Treasury is responsible for drafting guidance notes and since May 2015 the number of notes increased from five to over 50. The guidance notes are accessible and consistent. However, they would benefit from embedded hyperlinks to allow readers to quickly access other relevant documents and guidance notes, and it would be worthwhile for Treasury to consider either having an interactive flow chart for investors to determine what rules apply to them, or otherwise clustering the guidance notes into categories (for example, buying an established dwelling) to improve access to related information.

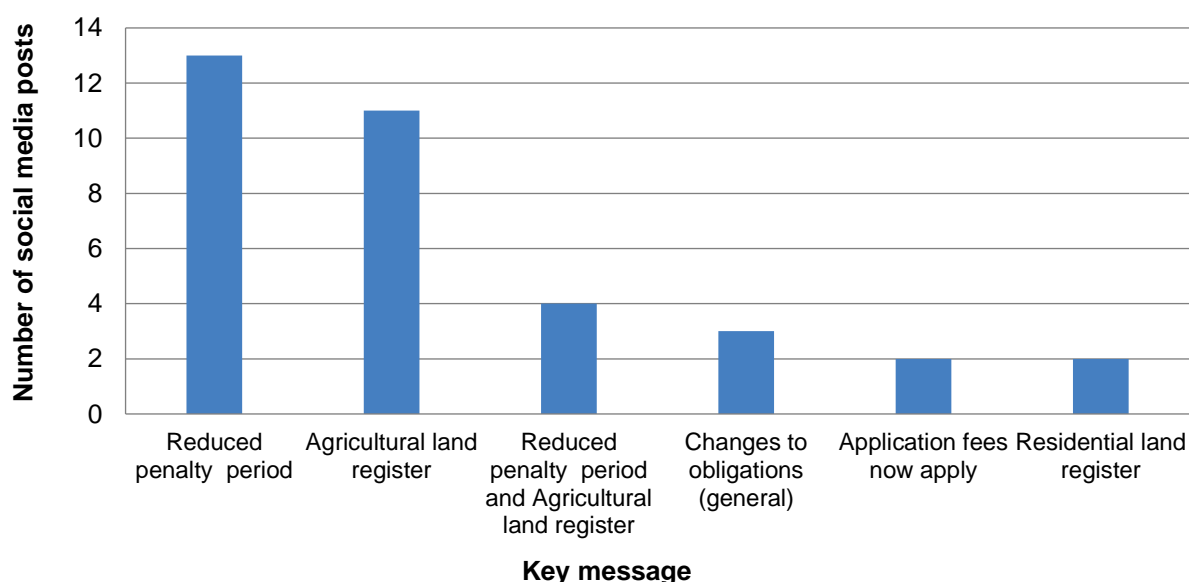
3.25 While guidance notes define how the legislation will work in most circumstances, the ATO and Treasury are not bound by them. There is a risk that the intended audience (both foreign investors and ATO staff) will perceive these as strict representations of the law. The ATO and Treasury should consider whether the status of these notes solely as guidance should be made clearer.

Social media and other campaigns

Social media

3.26 As illustrated in Figure 3.3, the ATO has used social media platforms to communicate key messages relating to foreign investment obligations, including for residential real estate. The messages included the introduction of new obligations, fees and penalties for foreign investors in residential real estate. From July 2015 to July 2016, the ATO made 16 tweets, 15 LinkedIn notifications, three Facebook posts and a YouTube video relating to foreign investment obligations. The ATO estimated that collectively these 35 posts reached more than 170 000 people.

Figure 3.3: Content of the ATO's foreign investment-related social media posts



Source: ANAO analysis of ATO documentation.

47 Foreign investment Review Board, *Guidance Notes*, [Internet], available from <<http://firb.gov.au/resources/guidance/>>[accessed 13 March 2018].

3.27 Since July 2016, the ATO has made no social media posts in relation to residential foreign investment obligations. The ATO advised that it would consider reinvigorating its social media presence in relation to foreign investment obligations for residential real estate.

Prompter campaigns

3.28 The ATO identified three types of prompter campaigns⁴⁸ in its risk treatment plan for foreign investment in residential real estate, and had commenced two of those by April 2018:

- notifying foreign investors who owned vacant properties of their obligations; and
- targeting investors who had acquired a property prior to seeking approval, requiring them to provide evidence to the contrary otherwise an infringement notice would be issued. A pilot conducted in early 2016 resulted in a 50 per cent infringement rate.⁴⁹

3.29 As prompter campaigns can be an effective method of encouraging voluntary compliance, the ATO should continue to consider this approach to address other compliance risks, such as the use of properties subject to redevelopment conditions.

Community and stakeholder engagement

Activities

3.30 Since July 2015, the ATO has conducted engagement activities to communicate to foreign investors their foreign investment compliance obligations.

3.31 The ATO conducted an *Understanding your Australian Taxation Obligations and Foreign Investment in Australia* program between October 2015 and June 2016. The program was co-designed with industry representatives, and aimed to present information to taxpayers and professionals to assist them to comply with their foreign investment and tax obligations.⁵⁰ It included nine community engagement events, in English and Chinese, which reached 1750 people.

3.32 The ATO also conducted a range of education sessions, seminars, presentations and webinars primarily aimed at intermediaries from 2015 to 2017. Audiences for these activities included solicitors, real estate agents and other government entities. Topics covered in these sessions included application fees, the land register and the ATO's compliance function.⁵¹ The ATO also set up information booths at events such as the Australian Business Forum.

Foreign Investment Reforms Working Group

3.33 The Foreign Investment Reforms Working Group was formed in July 2015 to develop and maintain ongoing relationships between relevant business and industry representatives and the

48 Prompter campaigns are where messages are sent through email to target audiences to emphasise particular obligations.

49 The ATO also conducted other prompter campaigns such as in relation to the residential land register. The campaign outlined in the risk treatment plan that had not been undertaken was to remind property developers of the reconciliation and reporting obligations associated with New Dwelling Exemption Certificates (refer paragraph 4.15). The ATO subsequently advised the ANAO that reminding property developers was done on a one to one basis each month and not on a campaign basis.

50 The program was specifically targeted towards the Australian Chinese community.

51 The webinars in 2017 generally focussed on the Register of Water Entitlements.

ATO.⁵² Currently the group meets quarterly, having met monthly from July 2015 to mid-2016. The working group was initially scheduled to cease in November 2016 but was extended at the request of the participants. The minutes of the working group are published on the ATO's website.

Residential foreign investment real estate help line and email inbox

3.34 The residential foreign investment real estate help line is a dedicated phone service for foreign investors, intermediaries and the general public to enquire about matters related to foreign investment in residential real estate. The help line is available from 8am to 6pm Monday to Friday, and there is also a residential foreign investment enquiries email address available to the public to submit queries.

3.35 Usage data from the phone service and email inbox are reported in monthly project status reports.⁵³ The ATO received approximately 400 calls per week in June 2017 and approximately 30 call centre escalations per week.⁵⁴ Email enquiries totalled around 80 per week for the period. Response timeframes are in place; however, adherence to these is not regularly monitored and reported.⁵⁵

Measuring the effectiveness of communication activities

3.36 The communication strategies outline an approach for measuring the effectiveness of communication activities, including reporting on letters sent, articles published, media articles generated, web analytics, webinar or roadshow feedback.

3.37 As illustrated in Table 3.4, the ATO's approach to measuring the effectiveness of communication activities has matured. The ATO's approach outlined in its 2017–18 plan includes communication objectives, deliverables and metrics. However, the metrics could be improved as they do not:

- identify targets or benchmarks to measure against; or
- specify qualitative indicators of success, such as whether foreign investors know where to go for assistance, and intermediaries are engaged and well-informed regarding residential real estate ownership for foreign investors.

3.38 In future communication plans, the ATO could include targets and benchmarks to measure improvement, and identify qualitative indicators that reflect the underlying intent of the communication activity.

52 Members of the group include the ATO, the Institute of Conveyancers, Real Estate Institute of Australia, and Chartered Accountants Australia and New Zealand.

53 Usage has been reported in the monthly Foreign Investment Screening Story since September 2016, and in the monthly Foreign Investment Program Status reports prior to that.

54 Call centre escalations are generally more complex queries referred to the residential real estate foreign investment team by the central ATO call centres.

55 Response times are five days for an email to the foreign investment mailbox and two business days for call centre escalations.

Table 3.4: Evaluation objectives and data sources of communication activities

| Year | Objectives | Data sources/communication metric |
|------|--|--|
| 2015 | Not identified | Reporting on the number of letters sent Publishing of articles Number of media enquiries Number of media articles generated Web analytics (such as page views and page hits) Responses/registrations by entities to direct mail-out Number of reduced penalty period disclosures, registrations on the land registrations Feedback from the Foreign Investment Reforms Working Group Stakeholder community engagement undertaken Reviewing and analysing call centre statistics |
| 2016 | Not identified | General reporting as outlined in the Marketing and Communication metrics data guide. Coverage and reach only Measure news and social media coverage and impact, including coverage, reach and sentiment |
| 2017 | Support the ongoing uptake of registrations to the water register of foreign ownership Support the introduction of new measures arising from the 2017 Federal Budget (vacancy charge) Refresh awareness of the overarching Foreign Investment Program, including agricultural and residential land, applications etc Ensure effective ongoing communications with foreign investors and their representatives so they are aware of the laws and their obligations. Internal communication activities to ensure ATO staff are aware of the Foreign Investment Program, the laws and what they mean for clients, and any impacts on their work | Visitors to ato.gov.au Media monitoring Visitors to Tax professionals newsroom article Social media Publication of articles through PR approach Webinar/Roadshow anecdotal feedback (if any) Media monitoring - internal |

Source: ANAO analysis of ATO documentation.

3.39 The ATO has prepared communication reports on a monthly basis since August 2016.⁵⁶ These reports include the results of those data sources outlined in Table 3.4 that have been undertaken.

3.40 The ATO evaluated one component of the communications approach in the form of a closure report for the *Understanding your Australian Taxation Obligations and Foreign Investment in Australia* sessions (see paragraph 3.31). The evaluation outlined effectiveness measures and identified information sources to inform measures.⁵⁷ In addition, the ATO mapped the behavioural impact of communication messages.

3.41 The ATO would benefit from undertaking a broader evaluation of the residential foreign investment communication program. In particular, it could assess the comparative effectiveness of activities including measuring the behavioural impact of messages. Such an assessment would enable a more informed approach for future communication strategies.

56 These reports outline the number of communication activities undertaken, such as social media and face-to-face activities, as well as key statistics including website activity. Due to reporting issues within the ATO, however, there are gaps in the coverage of all time periods.

57 These information sources include: registration and attendance; Q & A intelligence and audience feedback; a post session survey; and analysis mapping of public relations activities against registrations for the session.

4. Detection and investigation

Areas examined

The ANAO examined the effectiveness of the ATO's detection and investigation activities aimed at addressing non-compliance with foreign investment obligations for residential real estate.

Conclusion

The ATO has undertaken a significant amount of work to develop processes and systems to support the detection and investigation of non-compliance with foreign investment obligations for residential real estate. There are a number of minor enhancements the ATO could make to improve its largely effective investigation processes, with more substantial work required in its development of processes to actively detect non-compliance.

Areas for improvement

The ANAO made one recommendation aimed at the ATO developing and finalising data matching rules that address key compliance risks (paragraph 4.13). The ANAO also made five suggestions aimed at the ATO: aligning its case prioritisation framework with investigation outcomes (paragraph 4.21); introducing greater scrutiny of timeliness for compliance teams (paragraph 4.42); improving guidance available to assist compliance teams (paragraphs 4.36 and 4.44); recording recipients on the information gathering notice register (paragraph 4.47); and implementing an additional mechanism to review compliance team decisions (paragraph 4.49).

Are effective processes in place to detect non-compliance?

The ATO has partially effective processes to detect non-compliance with foreign investment obligations for residential real estate. It detected some 4300 cases of potential non-compliance from mid-2015 when it gained responsibility for compliance through January 2018, mainly from community or self-referrals or through approval processes for foreign investors. While the ATO has established a data matching program to actively detect non-compliance, as at April 2018 the program had not addressed all identified key compliance risks and more work was required to mature its processes for actively detecting non-compliance.

Information sources used to detect potential non-compliance

4.1 The ATO receives information relating to potential non-compliance through a number of sources, as shown in Table 4.1.

Table 4.1: Information sources for detecting non-compliance with foreign investment obligations for residential real estate

| Source of information | Description of source |
|------------------------|--|
| Self-disclosure | People who notify the ATO that they have breached the foreign investment framework. Notifications can be made through a form available on the Foreign Investment Review Board's website ^a or emailed directly to the ATO. |
| Community referral | The public can report suspected breaches of the foreign investment framework through a form available on the Foreign Investment Review Board's website. ^b |
| Other referral | Referrals from internal and external sources such as other ATO business lines, the media and local, state and Australian Government departments. |
| Screening infringement | Foreign investors identified through the foreign investment application process who indicate they have entered into unconditional contracts to purchase a dwelling prior to seeking approval. |
| Breach monitoring | The ATO's monitoring of people that have been provided the opportunity to remediate a breach of foreign investment obligations. |
| Data matching | The ATO's data matching program, which uses data from other Australian Government entities, state government entities and the private sector. |

Note a: Foreign Investment Review Board, *Self-disclosure form – residential real estate* [Internet], Foreign Investment Review Board, 2018, available from <<http://compliance.firb.gov.au/self-disclosure/>> [accessed 28 February 2018].

Note b: Foreign Investment Review Board, *Reporting a breach of the foreign investment rules* [Internet], Foreign Investment Review Board, 2018, available from <<https://compliance.firb.gov.au/compliance-reporting/>> [accessed 28 February 2018].

Source: ANAO analysis of ATO information.

4.2 From May 2015 through January 2018, the ATO reported receiving 4258 cases of potential non-compliance with foreign investment obligations for residential real estate, as indicated in Table 4.2. Of these, 3940 had been investigated and closed, with 318 cases remaining open and being investigated as at 31 January 2018.

Table 4.2: Number of total cases of potential non-compliance with foreign investment obligations for residential real estate per investor, by source of information, May 2015 through January 2018

| Source of information | New cases received | Closed cases | Cases remaining open |
|------------------------|--------------------|--------------|----------------------|
| Self-disclosure | 590 | 550 | 40 |
| Community referral | 1586 | 1557 | 29 |
| Other referral | 229 | 215 | 14 |
| Screening infringement | 1007 | 874 | 133 |
| Breach monitoring | 120 | 102 | 18 |
| Data matching | 726 | 642 | 84 |
| Total | 4258 | 3940 | 318 |

Source: ATO information.

4.3 Most cases of potential non-compliance with foreign investment obligations for residential real estate have been identified through the ATO receiving referrals (particularly community referrals and self-disclosures) or anomalies in approval processes. The ATO's data matching program is its primary active detection approach.

Use of data matching

4.4 The ATO undertakes data matching to detect non-compliance with foreign investment obligations for residential real estate, using its own data and data from other Australian government entities (such as the Department of Home Affairs and AUSTRAC), state government entities (such as New South Wales Fair Trading (Rental Bonds)) and private sector entities (such as banks).

4.5 The ATO obtains data from third-party entities through:

- formal/legislative arrangements where external bodies are required to report to the ATO. For example, banks are required to provide an Annual Investment Income Report to the ATO; and
- special purpose acquisition where the ATO obtains information from entities: using formal information gathering notices; under legislation that allows the other entity to provide the data; or voluntarily.

4.6 To develop data matching rules to detect non-compliance with foreign investment obligations for residential real estate, the ATO assessed potential compliance risks, as discussed in Chapter 3. The assessment included identifying 38 potential types of breaches and any relevant available data sets that could be analysed to detect those breaches.⁵⁸ The ATO identified 32 potential data matching rules⁵⁹ to detect the potential breaches. These were under varying stages of development as at March 2018, as shown in Table 4.3.

Table 4.3: Status of potential data matching rules for detecting non-compliance with foreign investment obligations for residential real estate, as at March 2018

| | Developed | Under development | Not started | Redundant | Under consideration | Total |
|----------------------------|-----------|-------------------|-------------|-----------|---------------------|-------|
| No. of data matching rules | 15 | 9 | 5 | 2 | 1 | 32 |

Source: ANAO analysis of ATO information.

58 For example, the ATO's assessment identified three potential breaches associated with approvals for construction on vacant land, including that for approvals made prior to 1 December 2015 construction does not commence within the two-year requirement period and the foreign investor fails to seek an extension. The relevant datasets identified to detect this breach are: real property data from state and territory land titles offices; the ATO's data on applications for foreign investment in residential real estate; Google maps; and the Department of Home Affairs' data on passports and citizenship.

59 Three of these rules do not align with potential breaches, including: approval breaches for datasets where a tax file number is held; identifying risk properties in a specific street or locality; and failing to apply new measures land titles data.

4.7 Those data matching rules under development at that time included some that were identified to detect serious compliance risks, such as:

- property purchased without approval;
- an Australian citizen or temporary resident purchased a property on behalf of a foreign investor; and
- property developers with New Dwelling Exemption Certificates⁶⁰ breached the conditions of their approval, including failing to market properties in Australia and failing to report to the ATO.

The data matching rules not started (or redundant/under consideration) involved more minor risks, such as a redevelopment failing to complete within four years.

4.8 At the time of audit fieldwork, the ATO was developing these data matching rules⁶¹ but more work was required to mature its processes for actively detecting non-compliance. The ATO had also not yet estimated the likely magnitude of non-compliance with foreign investment obligations for residential real estate, which would provide a basis for assessing and addressing compliance risks. The ATO advised in April 2018 that it would assess the likely magnitude of non-compliance when it had finished implementation and there was a reliable data set to draw from.

Detection of non-compliance facilitated by intermediaries

4.9 Intermediaries were identified as potential compliance risks in the ATO's risk assessment for foreign investment in residential real estate (see Chapter 3), but the ATO did not identify potential breaches in relation to intermediaries as part of its risk assessment and subsequently has not developed relevant data matching rules specifically targeting intermediaries.⁶²

4.10 While third-party details are captured by ATO systems, there is currently no guidance for compliance officers to record these details as part of investigations, which potentially limits the systemic data collection of the details of intermediaries that are linked to multiple non-compliance investigations.

4.11 The ATO has also identified intermediaries as potential compliance risks in the serious and organised crime environment, including in facilitating money laundering, other financial crimes and improper ownership in property. Analysing the ATO's foreign investor self-registration data for

60 A New Dwelling Exemption Certificate allows developers to sell new dwellings in specified developments to foreign investors without each foreign purchaser being required to seek their own foreign investment approval. From 9 May 2017 a condition on the certificates requires developers to sell a maximum of 50 per cent of the total dwellings in a development to foreign persons. A copy of the New Dwelling Exemption Certificate is provided to each foreign purchaser as long as their cumulative purchase interests in the development are below a total of \$3 million. If the total purchase interests exceed \$3 million the foreign investor will need to seek individual approval.

61 The ATO advised in April 2018 that it had further progressed a number data matching rules, including completing the data matching rule for property purchased without approval.

62 To January 2018, the ATO had conducted 13 investigations of intermediaries; of which 12 resulted in 'no further action' and one was put on hold pending the outcome of an investigation being undertaken in another section of the ATO. The ATO advised that investigations of intermediaries primarily stemmed from community and other referrals.

residential real estate, the ANAO tested a number of possible risk factors associated with 420 identified intermediaries, and identified:

- eight intermediaries that had assisted with purchases in three states and another 17 intermediaries that had assisted with purchases in two states; and
- 63 intermediaries that had assisted with ten or more purchases, including eight that had assisted with 50 or more purchases—of which 101 purchases was the largest number of purchases an intermediary had assisted.

4.12 The ATO advised that in January 2018 it appointed a complex case officer whose role is to examine intermediaries in a ‘structured manner’, including recommending potential changes to the ATO’s data matching to improve the identification of potential cases. The ATO also advised that its main focus for intermediaries was on education, as it considered that most breaches occurred after the involvement of an intermediary had ceased.

Recommendation no.2

4.13 The Australian Taxation Office prioritises developing and finalising data matching rules to address key compliance risks to foreign investment in residential real estate.

Australian Taxation Office’s response: *Agreed.*

4.14 *As the ATO has continued to develop its risk detection processes, further data matching rules have been finalised. The ATO will prioritise the continued development and implementation of outstanding data matching rules to address key compliance risks.*

Compliance reporting by developers

4.15 From 1 December 2015 to January 2018, the ATO issued 78 New (and Near-New) Dwelling Exemption Certificates.⁶³ A New Dwelling Exemption Certificate has a condition that requires developers to report to the ATO biannually from the date of issue until all dwellings in the relevant development are sold.⁶⁴ The ATO advised that as at 5 January 2018, 71 developers were reporting to the ATO and 726 of a potential pool of 23 170 dwellings has been reconciled.⁶⁵ Developers are

63 Near-New Dwelling Certificates relate to dwellings that have never been lived in but were sold and failed to settle. For brevity, the ANAO will refer to New and Near-New Dwelling Exemption Certificates collectively as New Dwelling Exemption Certificates.

64 The ATO advised that one month prior to a report being due, it will send a reminder to the developer, and if a report is not received on its due date, the ATO will phone the developer. Prior to the ATO assuming responsibility for this function, developers could apply for Advanced Off The Plan certificates from Treasury. Developers who have a reporting obligation in respect to these certificates continue to report to Treasury rather than the ATO.

65 Noting that from 9 May 2017 sales to foreign persons under an individual New Dwelling Certificate are capped at 50 per cent, the potential pool of dwellings reflects the total number of dwellings that were indicated on approved application forms submitted by developers. Four developers issued with New Dwelling Certificates had already been issued with Advanced Off The Plan certificates from Treasury and were therefore reporting to Treasury rather than the ATO. The remaining three developers who had been granted New Dwelling Exemption Certificates from the ATO no longer had reporting obligations as they had either already sold all dwellings or the development was no longer proceeding.

required to provide purchasers' full name, date of birth, current address, nationality, and details of the property sold, including its address, purchase price and date of sale.

4.16 The ATO advised that it manually checks the information reported by developers, including the sale price, number of dwellings sold and contract date. Based on the reporting submitted by the developer, the ATO calculates and advises the developer of the fee payable, which is due within 30 days of the reporting date.⁶⁶

4.17 As at 5 January 2018, the ATO advised that many developers that had been issued a New Dwelling Exemption Certificate had been required to report only twice and no developers had failed to report.⁶⁷ The ATO further advised that it had been working to educate developers and resolve any issues, such as payment of incorrect fees, and no developers had been issued breach notices or penalties to January 2018.

Are effective processes in place to address non-compliance?

The ATO has developed and implemented a largely effective program to address identified cases of potential non-compliance with foreign investment obligations for residential real estate in a limited time frame. Since gaining compliance responsibilities from Treasury in May 2015 through January 2018, the ATO completed 3940 investigations that identified 1158 breaches and resulted in 1067 financial penalties totalling some \$5.5 million, and the disposal of 231 foreign-owned properties valued at \$284.9 million. The key challenge for the ATO going forward will be addressing the more serious instances of non-compliance with the foreign investment framework; namely, demonstrating wilful non-compliance with obligations and applying criminal and civil penalties. There is also scope for the ATO to improve processes for escalating cases for investigation.

4.18 The ATO investigates all detected cases of potential non-compliance with foreign investment obligations for residential real estate—3940 of the 4258 potential cases or 92.5 per cent have been investigated from inception through January 2018. The remaining 318 remained open for investigation at that time (see Table 4.2).

Prioritising cases for investigation

4.19 To escalate cases of potential non-compliance for investigation by compliance officers, the ATO applies priority levels distinguished according to the source of information, as outlined in Table 4.4.⁶⁸

66 Developers are required to pay an initial fee of \$25 700 for a New Dwelling Exemption Certificate. For each dwelling subsequently sold to a foreign investor, the developer is required to pay the fee that would have been payable had the foreign investor sought foreign investment approval independently. Developers and foreign investors can reach an agreement in relation to who will pay the secondary fee.

67 There were initially limited numbers of New Dwelling Exemption Certificates issued after 1 December 2015 and therefore most developers were required to report twice after acquiring their certificates.

68 The ATO advised that compliance case work is also prioritised according to the probability that a risk will be identified and the need to maintain community confidence in the foreign investment regime by promptly investigating and/or responding to potential breaches in media reports or the offices of parliamentarians.

Table 4.4: Prioritisation for escalating potential cases of non-compliance with foreign investment obligations for residential real estate

| Priority | Priority level | Case source |
|----------|----------------|---|
| High | 1 | Self-disclosure |
| | 2 | Referrals other than community referrals, including from Parliamentarians, the Inspector General of Taxation, media reports and other intelligence sources ^a |
| Medium | 3 | Data matching cases with an expected disposal outcome ^b or Tier 2 outcome ^c Cases with a time limit ^d |
| | 4 | Data matching cases with an expected retrospective approval outcome ^e |
| Low | 5 | Community referrals ^f |

Note a: The ATO advised that requests from foreign investors to vary a condition for an existing foreign investment approval granted by Treasury prior to 1 December 2015 are treated with equal priority as these referrals.

Note b: The case selection team predicts the potential outcome of cases after profiling and assessing each case. To assess the potential outcome of a case, the case selection team determines whether a foreign investor has obtained a valid approval. If an approval is invalid, conditions noted in that approval are not legally enforceable and may warrant a different compliance treatment. An approval may be invalid where an application indicated a property had not yet been purchased when in fact it had, and the approval was issued before the *Foreign Acquisitions and Takeovers Act 1975* had been amended to allow retrospective approval in certain circumstances.

Note c: The ATO can issue an infringement notice for a Tier 2 penalty where non-compliance has been detected and confirmed through compliance activities rather than self-disclosure. A Tier 2 infringement notice is where the foreign investor has not notified the ATO of the alleged contravention of their foreign investment obligations prior to an infringement notice being issued. Tier 2 infringement notices incur higher penalties than Tier 1 infringement notices.

Note d: The ATO is required to apply a penalty within 12 months of a point-in-time breach; that is, where a breach is not continuing. An example of a point-in-time breach is where a foreign investor does not advise the ATO of a visa change within 14 days. An example of a continuous breach is where a redevelopment approval condition is that a dwelling remains vacant and the dwelling becomes occupied—the breach is continuous for the period the dwelling is occupied.

Note e: Retrospective approvals are generally granted where a foreign investor has purchased a property without approval but probably would have received approval had it been sought approval prior to purchase. The ATO advised that these cases would generally not be allocated if cases with an expected disposal outcome were available.

Note f: The ATO advised that the proportion of community referral cases that are confirmed as non-compliant is low and therefore these cases are a lower priority than other types of cases. Cases containing serious allegations may be prioritised for allocation.

Source: ATO information on prioritising compliance work.

4.20 In practice these priority ratings have not closely aligned with the case sources that have generated investigations with higher proportions of outcomes that demonstrate non-compliance. As discussed later in this chapter (refer paragraph 4.30), of all information sources, application screening had the highest proportion of closed investigations that resulted in a penalty (48.7 per cent); data matching had the second highest proportion (40.5 per cent) and self-disclosure the third highest proportion (39.3 per cent).⁶⁹ The ATO appropriately places community referrals as a low priority because the referrals do not often result in a non-compliance outcome. However, the

69 The proportion of closed cases that resulted in a penalty for the remaining case sources were: other referrals (8.4 per cent); breach monitoring (4.9 per cent); and community referrals (4.3 per cent).

ATO does not apply the same approach to the remaining sources. In particular, cases from other referrals⁷⁰ are considered to be a level 2 priority but only 1.8 per cent of those closed cases have resulted in a penalty.

4.21 The ANAO suggests that the ATO reassesses its approach to prioritising investigations into potential non-compliance with foreign investment obligations for residential real estate so that there is better alignment with investigation outcomes. The assessment could also include whether source of information remains the distinguishing criteria for determining priority levels, and clarify the purpose and use of the model used to prioritise cases, given that all cases are investigated.

Investigation outcomes

4.22 Where investigations find non-compliance with foreign investment obligations for residential property, outcomes include:

- disposal of property—either a self-disposal or forced disposal (type of penalty). Disposal orders are issued for forced disposal, where a property was acquired without approval and had approval been sought, it is likely that it would not have been granted;
- changed approval conditions—amendments to previously approved foreign investment applications, such as extension of time to redevelop land;
- infringement notices—which result in a financial penalty to investors.⁷¹ These are generally issued for minor offences including: acquiring a property without approval; failing to report the purchase of a property; breaching a condition of approval; purchasing property after the approval expires; and disposing of property to another foreign person without advertising it for sale in Australia;
- criminal or civil penalty—which can result in custodial sentences or financial penalties. These can apply to more serious non-compliant behaviour, for example where foreign investors knowingly breach the foreign investment framework;
- retrospective approval—where an investor did not apply for approval prior to purchasing a property but probably would have received approval had they applied⁷²; and
- screening breach—recorded for properties that have been acquired prior to approval and resulted in a Tier 1 infringement for the investor.

Where investigations do not find non-compliance with foreign investment obligations for residential property, no breach is identified or reported.

4.23 Of the 3940 closed investigations from May 2015 to January 2018, compliance breaches were found in 1158 cases (29.4 per cent). Of these breaches, 810 (70 per cent) were for failing to seek approval before entering a property contract and 348 (30 per cent) were of approval

70 Other referrals include those from parliamentarians' offices, the Inspector General of Taxation, media reports and other intelligence sources.

71 There are two tiers of financial penalties. Tier 1 penalties are applied where an investor self-discloses a breach and Tier 2 penalties are applied where the ATO uncovers the breach through investigation.

72 The ATO may issue an infringement notice in relation to foreign investors' failure to seek approval before purchase. From 1 December 2015 the ATO has required foreign investors to pay an application fee as penalty prior to the ATO providing the retrospective approval.

conditions.⁷³ A range of outcomes have arisen from those breaches, as shown in Table 4.5. Of note, in 231 cases the breach resulted in properties being sold, in 221 cases approval conditions were changed, and there were 350 retrospective approvals.

Table 4.5: Outcomes of investigations into potential non-compliance with foreign investment obligations for residential real estate, 2015–16 through January 2018

| | 2015–16 | 2016–17 | YTD 2017–18 ^a | Total |
|--|------------|------------|--------------------------|--------------------|
| Outcomes per property | | | | |
| Self-disposal | 15 | 66 | 75 | 156 |
| Forced disposal | 40 | 30 | 5 | 75 |
| Retrospective approval | 147 | 133 | 70 | 350 |
| Change of condition ^b | 59 | 93 | 69 | 221 |
| Screening breach | 45 | 227 | 84 | 356 |
| <i>Total breaches</i> | <i>306</i> | <i>549</i> | <i>303</i> | <i>1158</i> |
| Total number of cases investigated and closed ^c | 1637 | 1409 | 813 | 3940 |
| Outcomes for investors | | | | |
| Tier penalty ^d | 114 | 417 | 211 | 742 |
| Application fee penalty ^e | 20 | 127 | 103 | 250 |
| Criminal or civil penalty | 0 | 0 | 0 | 0 |

Note a: Year to date was to 31 January 2018.

Note b: Change of conditions refers to amendments to previously approved foreign investment applications.

Note c: The row and column totals do not reconcile for the total number of cases investigated and closed. Data for 2016–17 and 2017–18 YTD had not yet been published in a FIRB Annual Report and the ATO advised that the data was still to undergo verification and assurance processes.

Note d: Tier 1 penalties are when an investor self-discloses and Tier 2 penalties are where a breach is uncovered through ATO investigation.

Note e: Application fees payable for retrospective approval are reported by the ATO as a penalty.

Source: ATO information.

4.24 As the ATO has not estimated the size of the non-compliance pool, the proportion of potential instances of non-compliance that these investigations represent is unknown.

Imposition of penalties

4.25 Financial penalties can apply where non-compliance is found, including:

- Tier 1 and Tier 2 penalties, where there are differential penalties for individuals and companies, as outlined in Table 4.6;

⁷³ Breaches of approval conditions include: failing to use the property as a principal place of residence; renting out property that is required to remain vacant; failing to sell the property after ceasing to be a temporary resident; owning more than one established property as a temporary resident; foreign controlled companies illegally owning multiple established dwellings or failing to use dwellings for staff based accommodation; and developers failing to commence construction or redevelopment within required timeframes.

- disposal orders, which require the foreign investor to pay a penalty equal to the application fee that was appropriate to the value of the property, as outlined in paragraphs 4.33 and 4.34;
- retrospective approvals, which require the foreign investor to pay the application fee that would have been payable had they sought approval; and
- criminal prosecution and civil penalty orders, for contravention of sections 84 and 85, and section 94 of the *Foreign Acquisitions and Takeovers Act 1975* respectively.⁷⁴

4.26 As indicated in Table 4.5, to 31 January 2018 the ATO had imposed 1067 penalties in response to identified non-compliance with foreign investment obligations for residential property. These included 75 forced disposals of property, 250 application fee penalties and 742 Tier penalties but no criminal or civil penalties.

Infringement notices

4.27 Infringement notices were introduced as part of the foreign investment reforms on 1 December 2015. Infringement notices are generally issued for minor offences as outlined in paragraph 4.22, and can result in Tier 1 or Tier 2 penalties. Tier 1 infringement penalty amounts are 80 per cent less than Tier 2 infringement penalty amounts as illustrated in Table 4.6.

Table 4.6: Tier 1 and Tier 2 infringement notice penalty amounts

| Tier | Foreign entity | Penalty amount pre-1 July 2017 | Penalty amount post-1 July 2017 | Penalty units |
|--------|----------------|--------------------------------|---------------------------------|---|
| Tier 1 | Individual | \$2 160 | \$2 520 | 12 penalty units plus the relevant application fee |
| | Company | \$10 800 | \$12 600 | 60 penalty units plus the relevant application fee |
| Tier 2 | Individual | \$10 800 | \$12 600 | 60 penalty units plus the relevant application fee |
| | Company | \$54 000 | \$63 000 | 300 penalty units plus the relevant application fee |

Note: When a foreign person should have applied for approval to acquire the property and the application fee would have been paid as part of the application process, the application fee will be charged as a component of the penalty.

Source: ATO information.

4.28 As at January 2018, the ATO had issued 742 infringement notices for penalties totalling \$3.5 million, of which: 596 were for Tier 1 infringements and 146 were for Tier 2 infringements. Of the Tier 1 infringements, 71.3 per cent were identified through the screening process; 14.4 per cent were identified through self-disclosure and 10.2 per cent were identified through data matching.

⁷⁴ As at April 2018, the maximum criminal penalty for an individual was 750 penalty units (\$157 500) and/or three years imprisonment, and for a company the maximum criminal penalty was 3 750 penalty units (\$787 500). The maximum civil penalty is the greater of either: 10 per cent of market value of the interest in the property; or, 10 per cent of the consideration of the residential land acquisition. Amounts equivalent to the application fee may also be payable.

The majority of Tier 2 infringements (71.9 per cent) were identified through data matching, with community referrals accounting for 21.9 per cent of Tier 2 infringements.

4.29 The ATO's guidance on infringement notices is that a Tier 2 notice cannot be issued when a foreign investor has been contacted during the course of an investigation as this interaction is treated as a self-disclosure.⁷⁵

4.30 Financial penalties issued by the ATO from May 2015 to 31 January 2018 for non-compliance with foreign investment obligations for residential property totalled some \$5.5 million⁷⁶ as outlined in Table 4.7. All penalties were issued to foreign investors, and none to intermediaries or property developers. Further, the main sources of information leading to the penalties were: screening infringement (48.7 per cent); data matching (40.5 per cent); self-disclosure (39.3 per cent); and other referrals (8.4 per cent).

Table 4.7: Financial penalties issued by the ATO for non-compliance with foreign investment obligations for residential real estate, to 31 January 2018

| Source | Application fee | | Tier 1 | | Tier 2 | | Total | | |
|-------------------------------------|-----------------|------------------|------------|------------------|------------|------------------|------------|------------------|--------------|
| | No. | Value (\$) | No. | Value (\$) | No. | Value (\$) | No. | Value (\$) | Cases closed |
| Community information | 22 | 430 200 | 13 | 47 520 | 32 | 403 200 | 67 | 880 920 | 1557 |
| Data matching | 94 | 605 100 | 61 | 151 880 | 105 | 1 375 200 | 260 | 2 132 180 | 642 |
| Screening infringement ^a | 0 | 0 | 425 | 1 099 820 | 1 | 10 800 | 426 | 1 110 620 | 874 |
| Self-disclosure | 130 | 885 200 | 86 | 228 540 | 0 | 0 | 216 | 1 113 740 | 550 |
| Other referrals | 4 | 35 400 | 10 | 47 520 | 4 | 88 200 | 18 | 171 120 | 215 |
| Breach Monitoring | 0 | 0 | 1 | 10 800 | 4 | 45 000 | 5 | 55 800 | 102 |
| Total | 250 | 1 955 900 | 596 | 1 586 080 | 146 | 1 922 400 | 992 | 5 464 380 | 3940 |

Note a: Screening infringements are considered to be a self-disclosure and therefore only Tier 1 penalties are issued.

Source: ATO information.

4.31 To assist compliance officers in determining whether to issue a penalty, the ATO has developed guidance including a decision-making tree and an infringement decision matrix that identifies specific breach conditions and the relevant infringement timeframes.

4.32 Prior to the ATO gaining responsibility for managing compliance with foreign investment obligations for residential property, only criminal penalties applied under the foreign investment framework. The Treasury had not proceeded with any court prosecutions under the *Foreign*

75 Compliance officers are encouraged in the guidance to consider whether a Tier 2 notice can be issued prior to contacting the investor. Section 101(b) of the *Foreign Acquisitions and Takeovers Act 1975* specifies that a Tier 1 infringement applies if the person 'notified the Commonwealth of conduct that was the same, or substantially the same, as the conduct constituting the alleged contravention'.

76 Infringement notices result in a Tier 1 or Tier 2 penalty.

Acquisitions and Takeovers Act 1975 since 2006. In the *Foreign Investment Review Board Annual Report 2014–15* the Treasury reported one forced disposal and no penalty information.

Disposal orders

4.33 Disposal orders require the foreign investor to divest themselves of interest(s) in residential property. As at January 2018, 231 foreign-owned properties valued at \$284.9 million had been subject to disposal. Of these, 156 properties had been self-divested, 49 properties were a concessional disposal⁷⁷ and 26 properties were subject to disposal orders issued by the ATO. Of these properties, 39 per cent were identified through data matching, 30 per cent as a result of self-disclosure and 31 per cent through other sources.

4.34 The ATO's guidance is that if a foreign investor is issued a disposal order they should also be charged a fee equivalent to the cost of an application fee for the same property. As at 22 February 2018, the ATO advised that \$407 300 in disposal fees had been issued. The ATO's guidance instructs compliance officers to record disposal fees as Tier 2 infringements and advised the ANAO that this is because the relevant information technology system cannot separately record disposal fees. The ATO further advised that the system would be enhanced in 2018–19 to capture disposal fees and the guidance would be subsequently revised.

Civil and criminal penalties

4.35 Civil penalties were introduced in 1 December 2015 as part of the reforms to the foreign investment framework.⁷⁸ Existing criminal penalties were also increased as part of the reforms.⁷⁹

4.36 To date, the ATO has not applied any criminal or civil penalties. The guidance to staff indicates that for a criminal prosecution, the ATO must be able to establish that the foreign investor was aware of the laws and chose not to comply with them. However, the guidance does not indicate the type of evidence required to demonstrate that a foreign investor, intermediary or developer knowingly failed to comply with their foreign investment obligations or the method(s) for collecting that evidence. Further, the guidance does not indicate when a civil penalty would apply. The ATO could consider expanding guidance to provide its staff with more information on the application of civil and criminal penalties.

Payment and withdrawal of penalties

4.37 People who receive infringement notices can request an extension of time to pay the notice or request that the notice be withdrawn. Technical leaders are responsible for considering these requests and according to the ATO's guidance are instructed to review the reasons provided by the

77 As noted in Chapters 1 and 2, from 2 May 2015 to 30 November 2015 an amnesty was in place with concessional penalties for foreign investors, including a 12 month disposal period rather than a 90 day disposal period.

78 The civil penalty may vary according to the breach. For example, the civil penalty for purchasing property without approval is the greater of 10 per cent of the purchase price in addition to the relevant application fee, or 10 per cent of market value of the property in addition to the relevant application fee.

79 Criminal penalties increased from \$90 000 for individuals to \$157 000 (750 penalty units) for individuals for all relevant breaches including but not limited to: foreign person or temporary resident acquires property without approval; foreign investor purchases an established property or temporary resident acquires more than one established property; temporary resident fails to sell a property when it ceases to be their principal resident; and developer fails to complete constructions within four years without seeking an extension. Three years imprisonment can apply instead of the financial penalty.

person applying for the extension or withdrawal and to consider gathering further information where relevant.

4.38 The guidance for *Issuing infringement notices* encourages compliance officers to contact foreign investors who have been issued with infringements and who have not paid them within seven to 14 days to prompt payment. For unpaid infringements, compliance officers are instructed to send two reminder letters.

4.39 The ATO advised that it has not reported on the payment of penalties since August 2016 as tracking the timing was a manual and time consuming process, however the ATO advised that the majority of penalties issued have been paid as at January 2018.

4.40 Table 4.8 shows that \$4.5 million (82.4 per cent) had been paid of \$5.5 million in penalties issued.

Table 4.8: Payment and withdrawal of penalties at 31 January 2018

| Status of payment | No. of payments | Value of payments |
|---------------------|-----------------|--------------------|
| Payment outstanding | 37 | \$344 460 |
| Paid | 856 | \$4 538 680 |
| Withdrawn | 99 | \$583 760 |
| Total | 992 | \$5 466 900 |

Source: ATO information.

Investigation timeliness and support

Timeliness of investigations

4.41 The average time taken to complete an investigation is increasing, as shown in Table 4.9.⁸⁰

Table 4.9: Case management timeliness

| | 2015–16 ^a | 2016–17 | YTD 2017–18 ^b |
|--|----------------------|---------------------|--------------------------|
| Total no. of cases investigated (closed cases) | 1 637 | 1409 | 338 |
| Average investigation time | 35.9 days | 62.9 days | 80.4 days |
| Longest investigation | 286 days | 530 days | 540 days |
| Shortest investigation | 0 days ^c | 0 days ^d | 0 days ^e |

Note a: Cases were allocated to compliance officers from 29 July 2015.

Note b: Year to date was to 2 October 2017.

Note c: Seventy-two investigations were allocated and completed on the same day.

Note d: One hundred and thirty-two investigations were allocated and completed on the same day.

Note e: Two investigations were allocated and completed on the same day.

Source: ANAO analysis of ATO information.

⁸⁰ Timeliness was calculated from the recorded date the case was allocated to a compliance officer to the recorded completion date of the investigation.

4.42 The ATO advised that the change in case mix over time has contributed to longer average completion times. In particular, a greater share of earlier cases involved self-reporting of breaches, with relatively short completion times, while a higher share of late cases were from third-party referrals or data matching exercises, which required the collection and assessment of greater amounts of information.⁸¹ Notwithstanding these explanations, the ATO has not systematically reviewed the timeliness of cases with a view to measuring and encouraging efficiency. The ATO could also examine the causes of the longer investigations and possible remedies, and the accuracy of the reported shorter investigations, as outlined in Table 4.9.

Guidance for responding to non-compliance

4.43 When responsibility for investigating non-compliance with foreign investment obligations for residential real estate was transferred to the ATO in May 2015, there was limited guidance to assist compliance officers. Consequently, the ATO was required to develop a suite of guidance and templates to assist compliance officers to conduct investigations, including to correspond with people subject to investigations.

4.44 In a relatively short timeframe, the ATO developed internal guidance and templates to support most aspects of investigating non-compliance. The ANAO identified some areas for improving the guidance, as shown in Table 4.10.

Table 4.10: Potential improvements to the ATO's guidance for investigating non-compliance with foreign investment obligations for residential real estate

| Major improvements | Minor improvements |
|---|--|
| Introduce guidance on investigating intermediaries (refer paragraph 4.9). | Improve consistency of reference to current infringement penalties: <ul style="list-style-type: none"> • <i>Infringements – overview</i> indicates that there is one category of current penalties; and • <i>Procedure – Issuing infringement notices</i> indicates that there are two different categories of penalties: one that is applied for breaches occurring pre-1 July 2017; and one that is applied for breaches occurring post-1 July 2017. |
| Improve guidance on the application of civil and criminal penalties (refer paragraph 4.36). | Finalise the guidance on <i>Scripting Financial Institution Notices</i> that has been in draft since 2013. |

Source: ANAO analysis of the ATO's guidance documentation.

Information gathering notices

4.45 Compliance officers can seek information from other government departments and private sector institutions such as banks, utility providers and real estate agents. In its guidance on issuing information gathering notices, the ATO indicates that it prefers to use an informal approach in the

81 The ATO also advised that it changed the methods for recording cases on its case management system, with cases now remaining open until breaches were remediated, which has increased the measured time taken to complete a case.

first instance and apply the Commissioner of Taxation's formal information gathering powers when required.⁸²

4.46 From June 2016 through September 2017, the ATO issued 251 information gathering notices in relation to compliance with foreign investment obligations for residential real estate. Most notices were fully or partially complied with but a small percentage (nine per cent) were not responded to, as indicated in Table 4.11.

Table 4.11: Outcomes of information gathering notices in relation to compliance with foreign investment obligations for residential real estate

| | No. of notices with nil response | No. of notices with partial compliance | No. of notices with full compliance | No. of notices withdrawn | Total |
|--------------------------|----------------------------------|--|-------------------------------------|--------------------------|------------|
| 2016–17 | 6 | 1 | 164 | 0 | 171 |
| YTD 2017–18 ^a | 16 ^b | 5 | 56 | 3 | 80 |
| Total | 22 | 6 | 220 | 3 | 251 |

Note a: Year to date was to 30 September 2017.

Note b: These notices were due between 28 August 2017 and 18 September 2017.

Source: ANAO analysis of ATO information.

4.47 The ATO can prosecute people who do not respond to information gathering notices. While it is not likely to be appropriate to prosecute individuals or entities that fail to respond to a single information gathering notice, the ATO could give greater consideration to identifying and prosecuting individuals or entities who repeatedly fail to respond to notices.

Quality control

4.48 Team leaders and the technical leader provide a quality control mechanism in relation to the consistency of decision making and compliance approaches among compliance teams by approving the issuance of disposal orders, as well as the escalation of cases for criminal and civil penalties.⁸³

4.49 Team leaders are also responsible for approving the issuing of infringement notices, the escalation of cases for breach monitoring, approving cases that result in no compliance outcomes, and issuing information gathering notices, among other decision making responsibilities. There are two team leaders and their decisions are not reviewed, with the exception of when a process requires escalation to the technical leader. Without some review of team leaders' decisions, there is a risk of inconsistent decision making between the two teams. The ATO could consider a mechanism where a sample of cases are reviewed from each team at defined intervals to confirm consistency.

82 Compliance officers may invoke the Commissioner of Taxation's power to protect a third party from breach of privacy as it provides third parties with the legal means to provide information to the ATO. Information gathering notices are issued under sections 354 and 353 of the *Taxation Administration Act 1953*.

83 As noted in paragraph 4.36, the ATO has not applied criminal or civil penalties to date.

5. Monitoring and reporting

Areas examined

The ANAO examined the effectiveness of the ATO's and Treasury's monitoring and reporting on compliance activities for foreign investment in residential real estate.

Conclusion

Monitoring and reporting on compliance activities for foreign investment in residential real estate has been expanded with the transfer of responsibilities from Treasury to the ATO. Many indicators have been developed to measure the success of compliance activities and external reporting established for compliance investigations, outcomes and penalties. The monitoring and reporting arrangements are largely effective, and could be strengthened by more broad coverage of effectiveness—of the ATO in managing the overall compliance risk and Treasury in meeting the policy intent for foreign investment in residential real estate.

Areas for improvement

To further improve reporting on foreign investment and compliance activities the ANAO also suggests: the ATO establishes baselines and targets to improve internal and external reporting and its ability to assess the effectiveness of compliance activities (paragraph 5.5); and Treasury distinguishes between compliance activities conducted on agricultural investments and those activities conducted for residential real estate in the Regulator Performance Framework annual report (paragraph 5.18).

Do the ATO and Treasury measure the effectiveness of compliance activities?

The ATO has over 20 indicators of success for its compliance activities for foreign investment in residential real estate, which it has measured for inclusion in a variety of internal communication and compliance processes. However, the ATO has not yet used the results to broadly assess its effectiveness in managing the overall compliance risk that 'failure of foreign persons to comply with residential real estate foreign investment rules will undermine the integrity of the foreign investment framework and community confidence'. Similarly, Treasury has not measured effectiveness in achieving the stated policy intent of encouraging foreign investment in new residential dwellings.

Compliance objectives

5.1 As discussed in Chapters 3 and 4, the ATO manages elements of compliance with foreign investment obligations for residential real estate. The ATO's foreign investment in residential real estate risk treatment plan describes the overall strategy as 'aiming at increasing the transparency and visibility of our compliance activities to mitigate associated foreign investment risk ... and implementing treatment approaches to deal with identified risk.' The foreign investment risk is that 'failure of foreign persons to comply with residential real estate foreign investment rules will undermine the integrity of the foreign investment framework and community confidence.'

5.2 The ATO identified five desired outcomes in the risk treatment plan with 10 sources of data to inform indicators that will be used to evaluate if risk treatments have successfully achieved desired outcomes, as shown in Table 5.1.

Table 5.1: Risk treatment outcomes and evaluation data sources

| Risk plan outcomes | Number of success indicators in the evaluation template | Data sources |
|---|---|---|
| Participants apply for approval prior to acquiring an interest in residential real estate in accordance with the <i>Foreign Acquisitions and Takeovers Act 1975</i> . | 2 | <ul style="list-style-type: none"> number and trends in applications from risk participants website hits and statistics |
| Participants comply with approval conditions. | 3 | <ul style="list-style-type: none"> policy and communication initiative tracking |
| There is a sustained improvement by participants in applying and complying with foreign investment residential real estate approval conditions. | 4 | <ul style="list-style-type: none"> detect and deal – compliance activities desk based reviews data matched detected risk cases |
| Participants have an improved awareness and understanding of their foreign investment obligations in residential real estate. | 9 | <ul style="list-style-type: none"> external referrals from sources – AFP, AUSTRAC, ITX property, ATOi |
| Increased community confidence in the foreign investment framework and the ATO's ability to address compliance with residential real estate foreign investment rules appropriately. | 6 | <ul style="list-style-type: none"> internal referrals from ATO business lines self-reported disclosures community referrals |

Source: ANAO analysis of ATO *Risk Treatment Plan – Foreign investment in residential real estate*.

5.3 The indicators and associated data sources provide a framework for the ATO to monitor and report on the effectiveness of its activities to treat compliance risks for foreign investment in residential real estate.

5.4 One opportunity for improvement in the indicators is to establish more targets and measures against baselines. Approximately half of the success indicators (10 of 22) were described as counts of data for a point in time, which did not have associated targets or baselines. For example, the volume of self-reporting breaches could be improved if the indicator showed whether the volume was declining, or if the volume was a proportion of total breaches or defined by a threshold.

5.5 The indicators in the evaluation template are collated and reported disparately through internal communications and compliance processes.⁸⁴ As at April 2018, the ATO had not established baselines or consolidated the risk evaluation information collected to enable a broad view on the effectiveness of compliance activities. As such, the ATO had not clearly assessed the extent to which the foreign investment risk (noted in paragraph 5.1) was being managed. The ATO advised in April 2018 that the lack of historical information had limited its assessment of effectiveness, but

⁸⁴ Two indicators could not be found in any reporting: repeat offenders not identified for failing to apply or breaching conditions; and client experience of the application process.

going forward will consider establishing baselines to allow trends to be measured and measure effectiveness more broadly when there is a stable data set to draw from.

Policy intent

5.6 As discussed in Chapter 1, the stated intent of the foreign investment policy for residential real estate is to encourage foreign investment in new dwellings, thus increasing housing stock and supporting domestic job growth.

5.7 Treasury is responsible for implementing the policy on the foreign investment framework, however its responsibilities are broader than residential real estate, as indicated in Table 5.2.

Table 5.2: Treasury 2016–17 foreign investment related performance criteria and target

| | Performance criteria | Performance target |
|--|--|---|
| <i>Corporate Plan 2016–17</i> | The Treasury will aim to facilitate foreign investment to support economic growth, while ensuring that national interest concerns are appropriately addressed. | Performance will be assessed using the key performance indicators that have been developed under the Regulator Performance Framework for the Foreign Investment Review Board. |
| Portfolio Budget Statement Program 1.1 | Assessing foreign investment proposals | Number of proposals assessed |

Source: Treasury, *2016–17 Annual Report* [Internet], Treasury, 2017, available from: <<https://static.treasury.gov.au/uploads/sites/1/2017/10/Treasury-Annual-Report-2016-17.pdf>> [accessed 8 March 2018].

5.8 Treasury has not evaluated or reported the extent to which the stated policy intent has been met. The ANAO suggests that Treasury assesses and reports the extent to which the revised foreign investment policy objectives for residential real estate have been met, particularly with regard to the increase in new housing stock.

Do the ATO and Treasury effectively report on compliance activities?

The ATO and Treasury have largely effective arrangements in place to report on compliance activities for foreign investment in residential real estate, which could be strengthened by more broadly reporting on the effectiveness of those activities. The ATO has extensive internal reporting on compliance activities for foreign investment in residential real estate and shares this information with Treasury. The extent of coverage in the Foreign Investment Review Board's annual reports and Regulator Performance Framework reports has expanded since 2014–15, and includes information on compliance investigations, outcomes and penalties imposed.

Internal and inter-entity reporting

5.9 The ATO prepares various internal reports that contain information about its compliance activities for foreign investment in residential real estate, some of which are provided to Treasury, as outlined in Table 5.3.

Table 5.3: ATO internal and inter-entity reporting that covers compliance activities for foreign investment in residential real estate

| | Compliance report | Compliance story report | Public Groups and International site and function report |
|----------------------|---|---|---|
| Frequency | Monthly | Monthly | Quarterly |
| Information included | Case outcomes | Market demographics | Applications |
| | Cases by source and status | Breaches detected, including type, number and value of infringements issued, location of breach, nationality of offender and source of case | Number of compliance activities completed and number and value of penalties applied |
| | Number and value of penalties issued ^a | | |
| Audience | ATO staff and Treasury | ATO staff and Treasury | ATO Senior Executive Service officers |
| Commenced | August 2015 ^b | June 2016 | September 2016 ^c |

Note a: From April to August 2016, these reports included the value of penalties paid. However, the ATO advised that this reporting was discontinued as it was not required and the information was manually intensive and time consuming to gather.

Note b: The ATO prepared a high-level compliance report in May 2015, however, regular reporting commenced from August 2015.

Note c: Information about the ATO's foreign investment operations was first included in the Public Groups and International site and function July to September 2016 report.

Source: ANAO analysis of ATO information.

5.10 In addition to monthly compliance reports that the ATO provides to Treasury, it reports internally on foreign investment in residential real estate applications and collections on a monthly basis.

5.11 The ATO's reporting could be improved by including the value of disposal fees issued as well as the value of penalties paid, although its systems do not currently support the reporting of this information (refer Chapter 4). As discussed in the previous section, internal reporting could also be improved through the ATO establishing baselines and performance information to provide a broad view on the effectiveness of compliance activities.

External reporting

5.12 As shown in Table 5.4, the ATO and Treasury report limited information regarding foreign investment in residential real estate in their annual reports. However, the Foreign Investment Review Board's annual report includes information about the number of compliance activities, their source and outcomes.

Table 5.4: External reporting of compliance with foreign investment obligations for residential real estate

| Year | 2015–16 | 2016–17 |
|---|---|---|
| ATO annual report | Value of application fees collected | Value of application fees collected |
| Treasury annual report | Summary of achievement and the methods of achievement against the corporate plan performance criteria as outlined in Table 5.2 | Summary of the Regulator Performance Framework results against the performance criteria and targets set out in its <i>Corporate Plan 2016–17</i> and Portfolio Budget Statement Program 1.1 (refer Table 5.2) |
| Foreign Investment Review Board annual report | Residential real estate approvals by location, value and if approval was for established or new dwellings. Also residential compliance investigations and outcomes, and overall penalties information | Not applicable as the Foreign Investment Review Board had not published its annual report, as at 7 May 2018 |

Source: ANAO analysis of Treasury information.

5.13 Prior to 2013–14, the Foreign Investment Review Board annual reports did not include information on the outcomes of compliance activities, and this was acknowledged in the 2014 House of Representatives *Report on Foreign Investment in Residential Real Estate*.⁸⁵ Reporting was subsequently expanded in 2014–15 and 2015–16 as indicated in Table 5.4.

5.14 The release of public reporting on foreign investment has been slow and this was noted by stakeholders, including in relation to the Foreign Investment Review Board annual report for 2014–15 that was released 10 months later in April 2016. One stakeholder suggested that releasing quarterly datasets could allow timely analysis of key trends.⁸⁶ The 2015–16 annual report was released in late March 2017 and as noted in Table 5.4, the Foreign Investment Review Board annual report for 2016–17 was yet to be released in early May 2018.

5.15 The ATO annual reports have not included specific information on compliance with foreign investment obligations in residential real estate⁸⁷, although the amount of revenue collected in foreign investment application fees was reported for both years.⁸⁸ As stated in Chapter 2, the ATO

85 The House of Representatives Standing Committee on Economics enquiry found that Treasury could not provide concise information on: the operation of its hotline; the number of investigations it had undertaken since 2006; or how many voluntary disposals from temporary residents had occurred. Recommendation 2 was that the Foreign Investment Review Board and Treasury accurately capture audit, compliance and enforcement data. Treasury advised the ANAO that it had not developed key performance indicators during the period that it was responsible for compliance activities.

86 Additionally, in June 2014 the Reserve Bank of Australia released an article *Foreign Investment in Residential Real Estate* and concluded that data on foreign purchases is limited, more timely statistics could be published by the Foreign Investment Review Board, and that foreign developers influencing housing stock in Australia is difficult to determine.

87 The ATO advised in April 2018 that it does not include compliance information in its corporate annual report because Treasury owns this portfolio of work and the information is included in the FIRB annual report as a single source of truth.

88 The collection of foreign investment application fees began on 1 December 2015 and for 2015–16 the ATO reported collecting \$78 million in fees. For 2016–17 the ATO reported collecting \$134 million in foreign investment application fees.

aims to populate the register of foreign investment in residential real estate by December 2018 and prepare yearly reporting on the register once the states' and territories' information is standardised from 2019 onwards.

Regulator Performance Framework

5.16 The Regulator Performance Framework reporting requirements commenced on 1 July 2015⁸⁹ and two subsequent reports from the Foreign Investment Review Board have included information on foreign investment compliance activities. The ATO provides data for the Treasury to include in its reporting. Table 5.5 outlines the compliance activity information included in the Regulator Performance Framework reports.

Table 5.5: Compliance activities reported in Treasury Regulator Performance Framework reports

| | 2015–16 | 2016–17 |
|--|--------------|--------------|
| Number of matters referred for investigation | 2 104 | 1 669 |
| Number of properties required to be sold | 30 | 30 |
| Value of properties required to be sold | \$78 384 819 | \$34 304 889 |
| Number of penalties | 134 | 417 |
| Value of infringement penalties | Not reported | \$1 745 340 |

Source: Foreign Investment Review Board, Regulator Performance Framework report.

5.17 Treasury's Regulator Performance Framework reporting does not distinguish between agricultural land or residential real estate compliance activities. The reports include data for the single year reported and do not include previous years information.

5.18 The ANAO suggests that future reports could delineate between compliance activities conducted on agricultural investments and those activities conducted for residential real estate. Defining targets could assist the ATO and the public to understand if compliance strategies were effective, and including the information from past years would also provide visibility of trends over time.

Grant Hehir
Auditor-General

Canberra ACT
19 June 2018

⁸⁹ Nine Treasury portfolio agencies developed performance metrics in consultation with key stakeholders. The performance metrics were approved by Ministers in June 2015 and are being used by regulators in annual self-assessments of their performance against the Regulator Performance Framework.

Appendices

Appendix 1 Entity responses

Ms Lisa Rauter
Group Executive Director
Performance Audit Services Group
Australian National Audit Office
GPO Box 707
CANBERRA ACT 2601

Dear Ms Rauter

AUSTRALIAN NATIONAL AUDIT OFFICE PERFORMANCE AUDIT COMPLIANCE
WITH FOREIGN INVESTMENT OBLIGATIONS FOR RESIDENTIAL REAL ESTATE

Thank you for your email correspondence dated 9 May 2018 and for the opportunity to provide comments on the proposed report on the Australian Taxation Office's Compliance with Foreign Investment Obligations for residential real estate.

The ATO agrees with the two recommendations as presented in the section 19 report.

Attached is the summary of our comments to be included in the report (Annexure 1), the ATO response to recommendations (Annexure 2), and the editorial comments for your consideration (Annexure 3).

I would like to thank the Australian National Audit Office audit team for the cooperative and professional manner they have adopted in working with us on this matter. I look forward to continuing the good working relationship developed in this performance audit.

If you require further information on this matter, please contact Assistant Commissioner, Sophie Lewis on (02) 9374 8972.

Yours sincerely



Neil Olesen
Second Commissioner Client Engagement
Australian Taxation Office

Date: 4 June 2018



Australian Government

The Treasury

Matt Flavel
Acting Secretary

4 June 2018

Mr Grant Hehir
Auditor-General
Australian National Audit Office
GPO Box 707
CANBERRA ACT 2601

Dear ~~Mr Hehir~~ ^{Grant}

Proposed ANAO report: *Managing Compliance with Foreign Investment Obligations for Residential Real Estate*

I refer to your correspondence dated 9 May 2018 containing the proposed audit report, *Managing Compliance with Foreign Investment Obligations for Residential Real Estate*.

The Treasury welcomes the overall conclusions and findings of the audit.

While the report does not contain any recommendations for the Treasury, we will consider the key learnings identified within the report in the context of the Treasury's role in relation to administering the foreign investment framework, including our overarching policy responsibilities.

I am advised that the Australian Taxation Office, which has administrative responsibilities for foreign investment residential real estate compliance matters, will provide a substantive response to the report.

Thank you for the opportunity to provide comment on the proposed report.

Yours sincerely

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Matt Flavel
Encl.

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