THE PROPERTY INVESTMENT ASSOCIATION OF AUSTRALIA (P.I.A.A.)

Response to Questions in the Property Investment Advice Discussion Paper Ministerial Council on Consumer Affairs Working Party – August 2004

TABLE OF CONTENTS

Question One Page 4
What do you see as the key factors driving the growth in retail property investment in Australia in recent years?

Question Two Page 5
Have retail investors generally had a sufficient appreciation of the down-side risks associated with property investment? If you think a significant portion have not, can you suggest why this might be the case?

Question Three Page 7
How does the market for investment advice about property operate in Australia today? How are advisory services being provided and by whom?

Question Four Page 8
Is our characterisation of the seminar operators and investment promoters fair and accurate? If not, in what respects is it inadequate?

Question Five Page 9
In your view, are there significant problems associated with the property investment advice and training marketplace? If so, what are those problems and how extensive are they? What is the extent of consumer or investor detriment or loss?

Question Six Page 12
Is our characterisation of the problems associated with the property investment advice and training marketplace fair and accurate? Does it cover the main issues sufficiently? If not, in what aspects is it inadequate?

Question Seven Page 13
Leaving aside the unlicensed property investment promoters, are you aware of consumer problems associated with the property advice activities of professional or trade groups?

Question Eight Page 15
Do you have any comments on our outline of the current legal framework? Apart from those we have considered, are there any other laws or regulatory mechanisms relevant to the regulation of property investment advice and training activities?

Question Nine Page 16
Do you agree with the stated objectives of government intervention in the property investment advice marketplace? If not, what should governments' objectives be?

TABLE OF CONTENTS CONTINUED

Question Ten Page 17
Are the objectives referred to in the previous question currently being met?

Question Eleven Page 18
Can the objectives of government in relation to property investment advice be realised to an acceptable level within the current regulatory framework?

Question Twelve Page 19
If a new regulatory regime were to be introduced, what should its scope or coverage be? What activities should be covered, in respect of what types of property, and who should be protected? Do you agree that related advice about the financing of property investment should be covered?

Question Thirteen Page 20
If a new regulatory scheme were introduced, would a "carve-out" from the regulatory scheme be justified for any particular professional or trade groups, or in respect of any particular activities? If so, why?

Question Fourteen Page 21
Is there a role for self-regulatory or co-regulatory mechanisms (for example, a voluntary industry code or a mandatory code) in the regulation of property investment advice?

Question Fifteen Page 22
If a new regulatory scheme were to be introduced, how detailed and prescriptive should the scheme be? Are there particular regulatory requirements or mechanisms that should/should not be introduced? Should those involved in the provision of advice about property investment be required to be licensed?

Question Sixteen Page 23
What is your preferred Option among those outlined in section 9? Why? Are there other or variant Options that we should consider?

Question Seventeen Page 24
If a new regulatory scheme were to be introduced, should it be a Commonwealth or a State and Territory responsibility?

Question Eighteen Page 25
Is there other information you wish to provide? Are there other issues you wish to raise? Do you have any further comments?

QUESTION ONE

What do you see as the key factors driving the growth in retail property investment in Australia in recent years?

The greatest underlying factor over the past quarter of a century has no doubt been the increasing awareness by the public at large of the need to provide for retirement and the perception that property investment is a viable means of addressing this need. Following on from this has been the growth of property investment *as an industry*. The property development, property finance and financial planning industries are also focusing much more on retail property investment.

This growth, especially over the past 15 years, has been fuelled by a substantial increase in property values, Australia's fundamental economic strength, low interest rates and low inflation, the ready availability of finance, substantial demographic changes and the uncertainties associated with equity-based investments.

An increasing awareness of the tax deductions possible through property investment and the understanding that property can provide the investor employing such investment strategies with confidence and security have been paramount drivers in this respect. Both major political parties have shown themselves content to accept the strategy of gearing, for example, as a common business practice and are supportive of any means by which individuals can secure their future income in retirement.

The provision of rental housing is in great measure due to the existence and continuance of such treatment of these investor expenses and allowances.

Finally, over the past 10 years, the proliferation of the 'get-rich-quick' brigade, with its promises of making people 'millionaires in a minute, with no money and no risk', along with its aggressive marketing techniques, has obviously also had an impact.

QUESTION TWO

Have retail investors generally had a sufficient appreciation of the down-side risks associated with property investment? If you think a significant portion have not, can you suggest why this might be the case?

Have retail investors generally had a sufficient appreciation of the down-side risks associated with property investment?

The P.I.A.A believes that retail investors, before undertaking an investment, have generally not had sufficient appreciation of the downside risks associated with property investment. There has been insufficient disclosure of all forms of potential risks or volatility, including market volatility, possible deflation in property prices and negative movements on rental returns. Changes to lending ratios and valuations from those agreed to at purchase by major lenders have often been insufficiently detailed, with the result that investors have been less than fully informed about the extent of issues that can collaborate to cause capital loss in an adverse economic environment.

However, property investment is far more than the simple purchase of an investment property, and retail investors, long before the actual purchase of an investment property, are all too frequently uninformed or ill-informed about the more important fundamentals of a *property investment strategy*—for example, the need for conservative, careful and correct financial planning; knowing how to identify the right investment property; the role of time in a bona fide investment strategy. In other words, there has too often been a failure to develop property investment literacy in the first instance.

If you think a significant portion have not, can you suggest why this might be the case?

The P.I.A.A. believes that this has been and continues to be the case because of the lack of investment strategies, the influence of the 'get-rich-quick' brigade, and a substantial ignorance about property investment on the part of the general investment, finance and real estate industries. The reason that a number of property promoters, so-called 'wealth creation experts', do not provide this sort of information is that they are concerned that the consumer or potential purchaser may be put off by being introduced to the possible down-side consequences. Any negatives brought into a selling scenario would be perceived by those people as being counter-productive to their interests. Until some form of self-regulated response and minimum standards are introduced, these so-called 'get-rich-quick' experts will not undertake any form of detailed explanation as to volatility or risks, nor will they disclose secret deals or provide accurate information, on which an investor needs to rely when making an informed decision.

The P.I.A.A. insists on appropriate levels of disclosure on the part of all involved in the property investment cycle. Anyone advising retail investors on property investment should, as a matter of course, be able to impart appropriate information about general investment planning and property as an investment.

The P.I.A.A. submits that education standards and accreditation should be put in place to promote greater property investment literacy in advisors and consumers. Testing of the standard of competencies, including general investment principles, and a full education about the role and nature of property should be undertaken by participants in the property investment advisory function, but also not neglecting a major role for the property development, property finance and financial planning industries. The P.I.A.A. believes that some form of mandated Statement of Advice and minimum property investment education standard should be introduced so that retail property investors will consistently receive a detailed explanation of risks and disputation procedures.

QUESTION THREE

How does the market for investment advice about property operate in Australia today? How are advisory services being provided and by whom?

How does the market for investment advice about property operate in Australia today?

Market operations in Australia can be best described as unordered, if not chaotic at times. There is no structure or qualification system. The industry is an enigma, falling neither into the investment industry category, nor under the auspices of the property industry.

How are advisory services being provided and by whom?

The full spectrum of advice offered ranges from the experienced, specialist property investment advisor through to the property development world and the financial planning and finance industries, with advisory services being offered by accountants, solicitors, financial planners, developers, real estate agents and buyers' advocates. In-between lie many less-experienced and inexperienced investment advisors. 'Wealth creation' gurus, who come along in waves, it seems, and whose vested interests are often not appropriately disclosed to the consumer, serve merely to motivate people to undertake property purchases or to sell courses that promote speculation.

QUESTION FOUR

Is our characterisation of the seminar operators and investment promoters fair and accurate? If not, in what respects is it inadequate?

Is our characterisation of the seminar operators and investment promoters fair and accurate?

In general, the characterisation is fair and accurate. The P.I.A.A. is aware of the full spectrum of seminar operators and investment promoters, and as an association we are clearly concerned that dubious operators are creating an environment where ethical and experienced advisors are being brought into disrepute.

The danger, however, lies in over-generalisation and in tarring everyone with the same brush. Not all seminar operators or investment promoters have had a detrimental effect, yet there seems to be no real acknowledgement of the contribution and positive impact of bona fide, professional investment advisors.

If not, in what respects is it inadequate?

The dangers of over-generalisation are illustrated in the common usage of the term 'property spruiker', leading readily to the conclusion that seminars and workshops, educational programs and other forms of communication with the public are automatically bad and to be avoided. Of course this notion, embraced by certain sections of the media, is ridiculous.

Furthermore, it needs to be borne in mind that similar marketing initiatives and procedures are employed in other investment seminars—for instance, share trading—without, apparently, incurring the same criticism. We object to the seeming inference that property is tied up with every 'get-rich-quick' scheme.

The P.I.A.A. applauds the Working Group's efforts to ensure that appropriate standards are put in place. Marketing practices such as seminars, workshops and public presentations are universally recognised as legitimate means of communication, and can be and are conducted by professional, experienced and ethical operators in the property investment and financial education environment. These already adopt a process of ethical advice where the nature of the investments is accurately described and any possible downside risks are disclosed, ensuring that an uneducated potential investor is made fully aware of the contractual obligations they are entering into.

QUESTION FIVE

In your view, are there significant problems associated with the property investment advice and training marketplace? If so, what are those problems and how extensive are they? What is the extent of consumer or investor detriment or loss?

In your view, are there significant problems associated with the property investment advice and training marketplace? If so, what are those problems and how extensive are they?

The P.I.A.A. believes that there are indeed significant problems associated with the existing property and investment advice and training marketplace. This can relate to both the almost non existent training for property investment advisers as well as the plethora of public education seminars and the like.

For consumers, here is 'advice' given and 'training' offered that can never fall into the category of property investment advice. This includes exaggerated claims about the performance of property and so-called 'safe' investment strategies involving the use of mezzanine finance and 'wrapping', and so forth. This so-called investment advice can only be considered as speculation or trading.

Property investment advice and training can be good or bad. Promises of investors attaining millionaire status almost overnight with little effort or financial resources are unacceptable, and the P.I.A.A. frowns upon any consumer training program whose costs are excessive in relation to the likely outcome. The practice of charging absurdly high fees when the short-term outcome is negligible should be abolished.

Good, professional advice is to be promoted, while bad advice needs to be driven out, via qualifications, education, and appropriate self-regulation. A free seminar is fine if what attendees are being told is reasonable and realisable. There are many property investment advisors and education providers who work ethically and diligently as part of the advisory process—and often via free seminars and workshops in boardrooms and convention centres around the country. They go unnoticed. It is the bad news that gets noted.

Current regulation as it pertains to the investment industry has bypassed property. If property investment advice were recognised as a distinct industry, or at least a distinct financial service or product, it may have been covered under the Financial Services Reform Act. However, as a completely different asset class, property cannot be treated as one would treat securities, for example, and the expertise and experience acquired through a career in property is a world apart to that obtained in the securities and financial planning industries.

Likewise, how one understands and works with securities is far removed from how one would deal with and give investment advice with respect to property.

As part of its quest for the development of appropriate levels of consumer property investment literacy, the P.I.A.A. would welcome some form of appropriate regulation to protect the consumer from unethical and unreasonable behaviour. In this way, Australia will never again find itself in the position it has been in over the past decade.

The P.I.A.A. believes that a process of education in alignment with ASIC Policy Statement 146 needs to be introduced, where those who intend providing property investment advice, educational workshops and the like need to have successfully passed predetermined competencies developed by the industry for the industry. This would ensure the minimum necessary standard of education.

To address this situation, P.I.A.A. has sought the assistance of Deakin University through its commercial education division, DeakinPrime, to jointly design and develop a range of educational programs that align with the requirements placed on other sectors of the financial service industry. The primary target group is property investment advisors, for whom we have developed the P.I.A.A. Accreditation Program as a minimum educational standard that is aligned to the PS 146 training requirements elsewhere.

This accreditation program is part of a full Diploma in Property Investment, which is fully aligned to both PS 146 appendix A and B as well as the selected competencies under the Australian Qualifications Training Framework (AQTF). It will be developed by both commercial education and industry experts to ensure it has a high level of relevance and acceptance by participants.

We have also had several meaningful discussions with the Financial Services Education Advisory Authority (FSEAA ex NFITAB) to ensure this training will meet the needs of this industry.

The P.I.A.A. Accreditation Program will also provide pathways for other related sectors of the financial service industry such as financial planners, real estate agents, mortgage brokers and accountants. Eventually, this will help to ensure that consistent and appropriate property investment advice is received by consumers no matter where they go for such advice.

PIAA

What is the extent of consumer or investor detriment or loss?

We do not possess full information that allows us to quantify numbers; in fact, nobody does. However, let us bear in mind that such detriment or loss, to individuals, the community in general, as well as to the economy, is measurable in more than just monetary terms.

There are often significant lifestyle and family consequences as well as the loss of consumer confidence and trust in the industry professionals.

QUESTION SIX

Is our characterisation of the problems associated with the property investment advice and training marketplace fair and accurate? Does it cover the main issues sufficiently? If not, in what aspects is it inadequate?

The P.I.A.A. considers the characterisation of the problems to be fair and accurate, highlighting the dubious and unethical spectrum of certain sectors of the property investment and related industries. However, as has previously been mentioned, the problem areas alone are once again the subject of consideration. Our concern is for the industry, and for the future of the industry, so vital to the prosperity of our nation. There is a healthy property investment industry, as evidenced by the number of property investors in Australia, which is being tarnished by the same brush.

QUESTION SEVEN

Leaving aside the unlicensed property investment promoters, are you aware of consumer problems associated with the property advice activities of professional or trade groups?

Allow us to state first of all that we are not aware of any **licensed** property investment promoters.

The P.I.A.A. is, however, aware of a range of areas that could be tightened to protect the consumer. Some examples are:

- The manner in which property, especially off-the-plan developments, is marketed; what is presented or promised to the investor is not always attained in the final product.
- The sometimes inadequate documentation of contracts and plans
- The disparity between the finance approved at the point of purchase, particularly for off-the-plan contracts, and what is forthcoming at settlement
- The fact that issues related to the demand for tenancy and the time it takes to tenant a property are not always taken into account at the time of purchase.
- The extent to which tax deductions are appropriate
- The ability of investors to afford differing levels of gearing, both before and after tax.

In our view, there is no specific licensing process for the property investment industry and its advisors to ensure so-called experts are in fact experts. Until benchmark peer-developed accreditation is introduced into the property investment advisory industry, these practices will continue. A form of industry-mandated standards must be put in place.

The recently-registered and nationally-accredited Diploma of Property Investment that is presently being developed by Deakin University is aligned to both PS 146 appendix A and B as well as the selected competencies under the Australian Qualifications Training Framework (AQTF). The P.I.A.A will aim to set the appropriate educational and advice standards for the property investment industry and related sectors of the financial service industry. It is intended that the P.I.A.A. Accreditation Program, which forms part of the complete Diploma of Property Investment, shall be the minimum training requirement for those giving advice in property investment. We expect this accreditation program will become available during the first semester of 2005.

In addition, the P.I.A.A is presently establishing a Code of Conduct for its members, ranging from property investment advisors through to other professions and industries involved with property investment, including property developers, financiers, financial planners, accountants, and possibly the legal profession.

QUESTION EIGHT

Do you have any comments on our outline of the current legal framework? Apart from those we have considered, are there any other laws or regulatory mechanisms relevant to the regulation of property investment advice and training activities?

Do you have any comments on our outline of the current legal framework?

The framework in which we are presently operating is extremely difficult to comprehend. There are the big-picture regulations supervising the Corporations Act and FSRA (where the investment is defined as a financial service or product). As we have previously mentioned, property falls outside much of the FSRA. The ACCC is of course interested in misleading statements, unconscionable acts and the like. The operations of various State regulators, and particularly the Estate Agents Licence, which are State requirements, do not cover the property investment advisory process, or property investment as a whole. The P.I.A.A. believes there has been scope for dishonest and unethical operators who rely on the fact that there is a vacuum between regulation and correct commercial behaviour.

Apart from those we have considered, are there any other laws or regulatory mechanisms relevant to the regulation of property investment advice and training activities?

The P.I.A.A. asserts that investing in property is substantially different from investing in securities. However, frameworks and rules particular to property investment and similar to the requirements of the FSRA and ASIC PS 146 should be in place for those involved in the industry of property investment.

In addition, these regulations need to take into account other property investment services such as finance, tenancy management and property investment product, and the role played by property developers. These must be included in the framework.

QUESTION NINE

Do you agree with the stated objectives of government intervention in the property investment advice marketplace? If not, what should governments' objectives be?

The P.I.A.A. believes that the Government needs to create the legal framework in which industry associations such as the P.I.A.A. can operate in a self-regulatory mode. An industry association has the expertise to create policies and procedure guidelines, ethical codes of conduct, and the like. Government intervention does need to be introduced, whereby the current regulatory framework is looked at to ensure that there are no gaps between the federal regulators such as ASIC and the ACCC and those run by the various states.

The P.I.A.A. believes that a regulatory framework needs to be established in consultation with industry associations to create some form of policy statement regulation at the micro level. This should include education and training.

Together with Deakin University, the P.I.A.A. has created the Diploma of Property Investment, and an accreditation program in alignment with PS 146 for practitioners in the property investment advisory industries and other areas of commerce involved with property investment. However, without some form of regulatory requirement, only the interested and diligent will undertake such a program. This leads to inconsistency and leaves governments with the issue that the unscrupulous may not undertake the appropriate minimum industry training available.

The P.I.A.A. can provide the tools and organise the resources to set up expert practitioner standards of education, minimum standards of content for the advisory process, and policies and procedures, including Statement of Advice type documentation, for the use of investment advisors. However, unless a level of regulatory compulsion is introduced, the issues of concern in this White Paper will remain unresolved.

The benefits of such government regulation together with industry self-regulation should be obvious:

- It is preferable that the rules be made by those who own and believe in them.
- Since they make the rules, they will understand them—and know why they have made them!
- Those making the rules will also be vigilant in ensuring that the individuals and industries under their umbrella will abide by them.

QUESTION TEN

Are the objectives referred to in the previous question currently being met?

No.

QUESTION ELEVEN

Can the objectives of government in relation to property investment advice be realised to an acceptable level within the current regulatory framework?

No. (See our response to Question 9)

QUESTION TWELVE

If a new regulatory regime were to be introduced, what should its scope or coverage be? What activities should be covered, in respect of what types of property, and who should be protected? Do you agree that related advice about the financing of property investment should be covered?

A new regulatory scheme should be introduced at the national level, covering all types of property in which retail investors, as defined by this Discussion Paper, may choose to invest. Consumers should be protected in respect to all advice given in regard to investment in general and property investment specifically, the actual property to be purchased, and the financing of property investment.

Such a scheme should set the standards for the retail property investment process, which would include *product* and ancillary services, in particular finance and financial planning, as well as *advice*. Regulation should encompass product creation, investment planning, any marketing-based activity such as seminars, as well as point of sale and ongoing relationships. In this manner, people can expect certain minimum regulatory standards of advice, information, disclosure and property investment literacy to be provided in the process.

The nature of the regulatory framework, to the extent that it is appropriate for property investment, should be in line with the FSRA. Financial services and products that are property investments, and perhaps outside FSRA at this point in time, should have similar criteria and regulatory processes introduced to ensure identical, or very similar, rules and regulations are in place with respect to the nature of advice, educational standards and disclosure throughout the process. However, it must always be borne in mind, as we continue to emphasise, that property as an investment is fundamentally different to equity- and cash-based investments.

The P.I.A.A would wish to be part of the regulatory process to ensure that micro-issues, policies, procedures, the development of informative-type processes, guidance as to disclosure and minimum necessary educational standards are developed and implemented.

QUESTION THIRTEEN

If a new regulatory scheme were introduced, would a "carve-out" from the regulatory scheme be justified for any particular professional or trade groups, or in respect of any particular activities? If so, why?

The P.I.A.A continues to insist that since property investment is a distinct industry, it cannot and should not be regulated by existing sections of the property or investment industries, whose fundamental activities and knowledge base are far removed from property investment.

However, many individuals and professions do have an involvement in the property investment process. In our view therefore, in the first instance, there is a need for functionally-based regulation that would differentiate between the activities of such parties.

Some would argue that a carve-out should be available for those currently accredited through state regulation under the various Estate Agents Acts. However, the P.I.A.A. believes that there is little, if any, investment advisory training as detailed under FSRA in place for such graduates to receive a carve-out. Therefore we would recommend that no carve-out be available to estate agents where they seek to provide overall property investment advice (and it is the P.I.A.A's belief that estate agents will agree to this). For instance, there needs to be a line drawn at which estate agents would cease to give advice on the future performance of a property, or finance and financial planning advice in regard to property investment.

Secondly, there is a requirement for the establishment of an education and qualification-based scheme that recognises property investment as its own industry. The P.I.A.A. is cognisant of this, and its aforementioned Diploma of Property Investment will accord recognition for prior learning and experience, and offer concessional pathways into both the P.I.A.A. Accreditation Program and the full diploma. This should dispense with any need for carve-outs.

Those who do not receive a carve-out are those who cannot demonstrate any form of professional education or standards in property investment at this juncture. For those who have some form of PS 146 accreditation, be they financial planners, accountants or other professional investment advisory firms, the P.I.A.A. believes that their accreditation needs to be extended via the appropriate education and qualifications provided through the Diploma of Property Investment.

QUESTION FOURTEEN

Is there a role for self-regulatory or co-regulatory mechanisms (for example, a voluntary industry code or a mandatory code) in the regulation of property investment advice?

Clearly, there is not just a role, but a need for self-regulatory and co-regulatory mechanisms. Codes, policy and procedures, statement of advice-type requirements, disputation handling and other micro-issues best lend themselves to self-regulation by industry participants.

However, such self regulation needs to be supported by a regulatory requirement similar to that for other sectors of the financial service industry.

QUESTION FIFTEEN

If a new regulatory scheme were to be introduced, how detailed and prescriptive should the scheme be? Are there particular regulatory requirements or mechanisms that should/should not be introduced? Should those involved in the provision of advice about property investment be required to be licensed?

If a new regulatory scheme were to be introduced, how detailed and prescriptive should the scheme be?

The P.I.A.A. submits that the level of regulation required is relatively small.

We would suggest that there are two fundamentals to such a regulatory scheme. Firstly, government legislation needs to be enacted for national regulation of property investment. Secondly, it must be developed in such a way that it enables the industry's own association to accept responsibility for industry practice. Codes of conduct, industry guidelines, statements of advice, continuing professional development, accreditation programs, etc. need to be compulsory. This would create an environment in which participants recognise membership of an association by whose professional standards all members abide.

Are there particular regulatory requirements or mechanisms that should/should not be introduced?

In the fullness of time, specific regulatory requirements and mechanisms will evolve as a result of this Discussion Paper.

The P.I.A.A. would wish to be involved in the consultation process in this respect.

Should those involved in the provision of advice about property investment be required to be licensed?

The P.I.A.A. does not see how the property investment industry can be boosted professionally and ethically without such a form of qualification or accreditation.

QUESTION SIXTEEN

What is your preferred Option among those outlined in section 9? Why? Are there other or variant Options that we should consider?

The P.I.A.A. believes that self-regulation through an industry association can operate to solve most of the concerns expressed in this Discussion Paper. However, for a standard of behaviour to be set and for recalcitrants to be brought into line, a regulatory framework needs to be established. Such a framework would detail the broad aspects and nature of the process of advice within the property investment industry advisory area, and would also, as we have outlined, encompass investment product and ancillary services, in particular finance and financial planning. The minutiae would be determined by the industry association.

This means that the P.I.A.A's preferred position is somewhere between Options 2 and 3, a solution where the property investment advice law works across Australia with no possibility of variation in any state. While the framework is being put in place, educational standards (similar to PS 146), the minutiae of investment advice policies, disclosure required, etc. can be determined by industry participants.

In terms of adjustments to this regulatory framework, there could be a number of professions and industries currently regulated by state law, for instance, the estate agency industry, which will need to be brought under the umbrella of the new national regulations.

QUESTION SEVENTEEN

If a new regulatory scheme were to be introduced, should it be a Commonwealth or a State and Territory responsibility?

The P.I.A.A. believes that the process of licensing and co-regulation should operate at the federal level through ASIC via an AFSL-type mechanism and general policy statements, under which the industry association will self-regulate.

QUESTION EIGHTEEN

Is there other information you wish to provide? Are there other issues you wish to raise? Do you have any further comments?

The P.I.A.A believes it has carefully and fully responded to all the questions put by the Property Investment Advice Working Party and has raised those issues it deems important to the interests of consumers and the relevant industries.

Representatives of the P.I.A.A would welcome the opportunity to appear before the Working Party prior to the final Report being written and made publicly available.