

5 November 2007

Kerryn Riseley  
Executive Officer  
Victorian Parliament Law Reform Committee  
Parliament House  
Spring Street  
MELBOURNE VIC 3000

Submission No. PI/14  
Received 9 November 2007  
Law Reform Committee

Dear Ms Riseley

**RE: LAW REFORM COMMITTEE INQUIRY INTO PROPERTY INVESTMENT**

Please find enclosed the Australian Property Institute's (API) submission to the Law Reform Committee Inquiry into Property Investment.

The Australian Property Institute (Victoria Division) Inc. (API), is a representative professional organisation specifically formed to meet the needs of Property Professionals and present a professional view on property issues in public forums. Established in 1927, the API is genuinely multi-disciplinary in its property focus and membership.

The API is a non-profit, non-political, independent professional association. Our organisation serves the needs of professionals as specialists and as contributors within the broadest sphere of property. It also caters for the particular needs of individuals seeking to enter the property profession. The API requires its members to undertake continuing professional development, observe API professional standards, including a Code of Ethics and Rules of Conduct.

The API believes there needs to be greater regulations for property investment professionals to ensure appropriate qualifications, standards and experience are at a level to meet the needs of the Australians and in this particular case, the Victorian community.

A good case study is the mid-1990's disbanding in Victoria of the Valuers' Qualification Board appointed under the Valuation of Land Act 1960. This removed the requirement for formal registration of property valuers and as such, a person with no qualifications or training anyone can provide property advice and hold themselves out to be a property valuer. This has removed a public safety feature and adds confusion to the public and increases the potential for exploitation of potential investors in direct property and/or related schemes.

Our submission is based on the particular desire of the Victorian Government to minimise the exposure to exploitation of Victorians in making real property investments (or associated schemes) based on unsubstantiated and imprudent property advice in the context of keeping the burden on business as low as possible. The API's preferred outcome is to minimise avoidable conflict before investments are made by mums and dads rather than deal with the drawn-out legal ramifications of litigation when things go wrong, with the obvious negative impact on society. The API does not believe the current AFSL licensing regime is appropriate for all property professionals, but would rather see the API be recognised as an appropriate home for independent property investment professionals. This would ensure a minimum educational standard, compliance with a code of conduct and ethical standards, continuing professional development and a disciplinary process.

## **Structure of API Submission**

This submission is structured as follows:

1. What constitutes Property Investment advice?
2. Why is regulation of Property so important?
3. Key issues for the Property Investment advisory industry.
4. Concluding messages from the API.

### **1. What constitutes Property Investment advice?**

The essence of this section is to:

- a) Distinguish between Property Advice and Vendor Representations
- b) Distinguish between Real Property and Securitised Property
- c) Distinguish between Property Investment Advice and Other Property Advice.

#### Property Advice vs Vendor Representations

The API believes it is important to distinguish between property advice and “spruiking” or “marketeting”, often made by vendors of real property or schemes related to real property.

Independent property advice should be provided only from suitable qualified, highly experienced people who are skilled in the subject matter and are regarded as experts by the property industry and market peers. Spruiking or marketeting is often associated with developers or other compromised people or entities who will directly profit generally from transactional based activities. The latter activities are not independent due to the obvious vested interests of those concerned.

The real issue is the public is often “hoodwinked” or misguided into attending seminars, market briefings or other apparently legitimate, information sessions that are merely masks for the true motives of these parties.

The API believes there needs to be requirements imposed on vendors and/or their agents and marketing personnel advising all potential investors to seek independent property advice before making an investment.

#### Real Property vs Securitised Property

The API's focus in this submission relates primarily to investment advice given in relation to real property not advice on securitised property investment products (e.g. units in listed and unlisted property investment schemes). The latter type of investment is already highly regulated under the Australian Financial Services Reform Act (AFSR) administered by ASIC and requires participants in this industry to have a financial services licence.

The regulatory environment governing advice on real property is relatively benign, evidenced by the example of the de-regulation of the real property valuation industry in the mid-1990's.

The API strongly believes there should be increased regulation of real property investment advisors to provide clarity for the general public when dealing in the industry. A licensing regime, not dissimilar to the requirements for certain trades, that is governed by legislation imposing serious penalties for unprofessional conduct, would achieve a heightened awareness by the public of those individuals or entities purporting to be something they are not. The regulation would require full disclosure of conflicts of interest or pecuniary interests

in properties (or related schemes) being marketed by vendors or their representatives which are being “disguised” in the form of information sessions.

Misleading and deceptive conduct is obviously governed by the Commonwealth’s Trade Practices Act 1974 and Victoria’s Fair Trading Act 1999, however these laws do not require individuals to disclose either the potential financial risks to investors, conflicts of interest (e.g. receiving commissions) or other pecuniary interests.

### Property Investment Advice vs Other Property Advice

The API’s main concern relates to real property investment advice, not the myriad of other advice available to the investors including legal advice, quantity surveying advice or town planning advice to provide some examples.

The following table broadly summarises the Property Investment Process and highlights the need for advice across its various stages:

Ownership Stage	Service Available	Typical Provider
<b>1. Acquisition</b>	<ul style="list-style-type: none"> <li>- Decision to invest in Real Property</li> <li>- Negotiation</li> <li>- Due Diligence Review               <ul style="list-style-type: none"> <li>- Legal (title &amp; contracts)</li> <li>- Physical</li> <li>- Financial Reporting &amp; Tax</li> <li>- Planning</li> <li>- Environmental</li> </ul> </li> <li>- Valuation</li> </ul>	<ul style="list-style-type: none"> <li>- Financial Planner/Asset Allocator</li> <li>- Real Estate Agent/Solicitor/Property Advisor</li> <li>- Solicitor</li> <li>- Engineer/Architect</li> <li>- Accountant</li> <li>- Town Planner</li> <li>- Environmental consultant</li> <li>- Certified Practising Valuer</li> </ul>
<b>2. Holding</b> ↓	<ul style="list-style-type: none"> <li>- Property Management &amp; Leasing</li> <li>- Financial &amp; Taxation</li> <li>- Development</li> <li>- Valuation, Rating &amp; Compensation</li> <li>- Investment Analysis</li> </ul>	<ul style="list-style-type: none"> <li>- Real Estate Agent</li> <li>- Accountant</li> <li>- Architect/Builder/Quantity Surveyor</li> <li>- Certified Practising Valuer</li> <li>- Certified Practising Valuer</li> </ul>
<b>3. Disposal</b> ↓	<ul style="list-style-type: none"> <li>- Marketing &amp; Negotiation</li> <li>- Contracts</li> <li>- Valuation</li> </ul>	<ul style="list-style-type: none"> <li>- Real Estate Agent / Property Advisor</li> <li>- Solicitor</li> <li>- Certified Practising Valuer</li> </ul>

### Key Points

- a) Property investors can access various types of property services throughout the property investment life cycle. These services are provided by specialist property service providers.
- b) Investors will seek these services dependent upon the extent of their own property expertise and the complexity of the particular property investment.
- c) The key investment advice often relied upon by both equity and debt investors is an independent current market valuation of the property. Often this is a constitutional requirement, particularly for trustees and financiers.

- d) This independent valuation advice involves an unbiased assessment of the financial rewards and risks from property ownership, taking into account all available information (including due diligence reports) available on the respective property.

The broad membership base of the API, predominantly comprising valuers, land economists and investment consultants, is integral to the real property investment process, highlighted by the table above and the key points that follow. The API is therefore well positioned to play a pivotal role in any reforms emanating from this Inquiry.

## 2. Why is regulation of Property so important?

The following table highlights the prevalence of the various forms of property investments in our community:

### Estimates of private investment in property

Property Type	Equity \$bn	Share %	No.
Investment property directly owned	200	80%	1,900,000
Listed property trusts - retail investors	16	7%	520,000
Syndicated & unlisted property trusts	5	2%	140,000
Property securities - retail investors	13	5%	260,000
Mortgage funds	15	6%	250,000
<b>Total private property investment</b>	<b>249</b>	<b>100%</b>	<b>3,070,000</b>

Source: Property Investment Research 2004

Real property represents a significant proportion of the invested and investible capital in our community. Whether this takes the form of direct investment in real property or an investment in a product or scheme whereby the key income and capital returns are derived from real property, the need for independent investment advice on the real property is paramount.

A number of investment products or schemes can be "dressed-up" through financial structuring, in order to make that particular product or scheme more appealing to potential investors than its competitors. However, if investors received independent advice from appropriately qualified and experienced property investment professionals, they will quickly be able to assess the difference between the "headline" forecast returns (obtained via structuring which increases the risk of financial loss) and the underlying forecast returns which are derived from the real assets underpinning the product or scheme.

The need for increased regulation of property investment advisors is critical given the level of exposure the broad community has to this asset class.

## 3. Key issues for the Property Investment advisory industry.

There are a number of issues currently affecting the Property Investment advisory industry. These are outlined as follows:

- a) **Inadequate Regulation** - Property investment professionals are not adequately licensed or regulated, thereby allowing exploitation of the Australian public by unscrupulous, undisciplined people who only care about increasing their wealth by using "mum and dad" investors' capital. The API believes a national approach, similar to ASIC's regulation of managed investment schemes, is preferable. There

may be an opportunity to join with state based industry bodies to cover issues peculiar to state legislation as it affects real property.

- b) **Confusion over who is appropriately qualified** - The broader community is confused about who is properly qualified and experienced to provide independent property investment advice. Some members of the public perceive professionals such as real estate agents and other "commission-based" services as the only available property advisors. It is difficult to argue that real estate agents are independent in their advice (either on the buy-side or the sell-side) because their commission is usually linked to a transaction. Independent property advisors are paid a fee for service and are disinterested in whether a transaction proceeds or not. A higher profile for regulated independent property advisors would remove the current confusion and provide investors with confidence about the reliability of the advice.
- c) **Unqualified Financial Planners** - Members of the Financial Planning industry, whilst an obviously legitimate part of the investment landscape in Australia, are not suitably qualified (unless the requisite tertiary education course has been completed and minimum experience requirements have been met) to provide advice on real property. This point is linked to the one above about the current confusion in the broader community.
- d) **Vendor Marketing** - There have been calls for property developers/vendors selling their own property directly or through an agent to be licensed. The API does not believe such developers or vendors need to be licensed themselves. Preferably, there would be minimum disclosure requirements on the vendor (e.g. agents to disclose the capacity in which they are acting and the benefit they will receive) and the ongoing licensing/registration of real estate agents. However, the API believes that developers should not be able to charge interested parties to attend marketing events/functions whose purpose is to sell property. This is to avoid the potentially confusing perception that such events are educational in nature. These developers or vendors should be required to prominently disclose that potential investors should seek their own property investment advice before committing.

#### 4. Concluding messages from the API.

The API firmly believes this Inquiry represents a unique opportunity for the Victorian Government to lead the nation in raising the bar on the control required in the real property investment advisory industry.

The API submits that:

- a) Property investment advice should only be provided by independent, appropriately qualified and experienced people who deal with real property on a regular basis. For example, with the de-regulation of the property valuation industry (a critical and majority sector of the property investment advisory industry), professional standards in that industry have declined, despite the best efforts of the API. The reason is the "blurring" of who a truly qualified valuer is given that industry's de-regulation and the obvious exploitation of that by industry participants with vested interests.
- b) There is an increased need for reliable, independent property advice in the community given the high exposure of the Australian household capital base to this asset class. This need is increasingly required in a more volatile, inflationary global

financial system. Obviously, the bull market of the past 15 years has “hidden” many sins by property investors, advisors and other market participants. The future will require property professionals to draw on all of their education, training and experience to manoeuvre through the next part of the investment cycle.

- c) Regulation and/or licensing of real property investment advisors will provide clarity for the public and will strengthen the credibility of the asset class by removing the ability for unprofessional conduct by parties with vested interests. The current “self-regulation” system does not carry the same weight as legislative control of this important industry. The API believes that the Victorian Government should either:
- Reintroduce the minimum educational and experience requirements supported by registration or licensing requirements, or
  - Support the API in self regulation of the industry by requiring persons wanting to provide property investment advice be (as a minimum) Associate Members of the API.

The API believes it is the pre-eminent industry body to represent the property investment professionals required to be regulated/licensed under our proposal because of:

- a) The API's stringent requirements for Associate membership

All applicants for Associate Membership must have completed an API accredited degree or a graduate diploma with an approved prior academic qualification. They must also have had two years approved professional experience and must sit a Professional Interview conducted by the API Panel of Examiners.

- b) The API's high standards in governance:

The API is committed to implementing and maintaining an effective and comprehensive Corporate Governance policy. The policy, practices and procedures have been developed in accordance with the Australian Standard *Good Governance Principles* (AS 8000-2003) and provide a measure of protection to all parties involved in the various property processes. The Code of Professional Practice sets out the duties, responsibilities and professional standards of API members. Guidance notes, practice standards and technical papers are recognised nationally and internationally. The API has an internal audit processes for professional development and risk management as well as a Complaints Procedure under the Constitution.

- c) The API's on-going professional development requirements of its members

Graduate, Associate and Fellow members of the API must undertake 20 Continuing Professional Development (CPD) points per annum. All members who undertake valuations of real property must attend an Institute approved Risk Management Module every three years.

- d) The API's high ethical standards

The API's Code of Ethics is a public statement of the principles, value and behaviour expected of Members of the API and approved of by the ACCC. It relates to compliance with standards, professional duty, competence, conflict of interest confidentiality and the profession. The API continually promotes the significance of its Code of Ethics, interpreted and expanded in the Rules of Conduct, which are mandatory for all Members.

- e) The API's Professional Indemnity (PI) Insurance requirements of its members

The API advises and assists its members in achieving an appropriate level of PI Insurance. The API believes its Risk Management Module, mandatory for those members undertaking valuations of real property, helps in keeping PI Insurance costs down.

f) The API's independence

The API ensures its independence is maintained and while it does foster kindred body relationships it never compromises this independence or that of its members. Reciprocity agreements exist with several comparable Institutes overseas and the API standards align with the International Valuations Standards. API membership is done on an individual and not corporate level and any association with another kindred body would be limited so as to always preserve its independence and avoid undue influence.

The API would be pleased to provide further information in relation to this submission if requested,

Yours faithfully,



Milton Cations FAPI  
President  
API Victorian Division