SUBMISSION

TREASURY LAWS AMENDMENT (REDUCING PRESSURE ON HOUSING AFFORDABILITY MEASURES (NO.2)) BILL 2018

FOREIGN ACQUISITION AND TAKEOVERS FEES IMPOSITION AMENDMENT (NEAR - NEW DWELLING INTERESTS) BILL 2018

Submitted by:

National Affordable Housing Consortium (NAHC)

Sustainable Living Infrastructure Consortia (SLIC)

Griffith University Business School

To,
Committee Secretary,
Senate Economics Legislation Committee,
PO Box 6100,
Parliament House,
Canberra, ACT 2600

7 March 2018

From,
Mike Myers,
National Affordable Housing Consortium,
1/118 Vulture Street,
South Brisbane, QLD 4101

Re: Senate Economics Legislation Committee- Invitation to submit to the inquiry into Treasury Laws Amendment

Dear Mark,

Thank you for giving us the opportunity to make a submission on the following proposed amendments: Treasury Laws Amendment (Reducing Pressure on Housing Affordability Measures (No.2)) Bill 2018 and Foreign Acquisition and Takeovers Fees Imposition Amendment (Near- new Dwelling Interests) Bill 2018. This submission is made by the National Affordable Housing Consortium and its research & development company, the Sustainable Living Infrastructure Consortium, and includes working-party support from Griffith University Business School.

In our submissions, we have addressed the scope of the proposed legislation, including technical issues around foreign investment. We have also addressed the issues around the CGT proposals and find that they are a totally inadequate facility to add substantial value to affordable housing provision. In addition, because these issues are connected, we have resubmitted our previous submission to Treasury regarding Managed Investment Trust legislation for contextual consideration in relation to affordable housing. You may consider this out of the scope of your review, but we have attached it for your information.

Please find our submissions enclosed:

SUBMISSION 1: Policy Context and Submission Overview: (1A) Submission on Treasury Laws Amendment (Reducing pressure on Housing Affordability No2) Bill

2017 and Income Tax (Managed Investment Trust Withholding) Amendment Bill 2017and (1B) Detailed Report on that Submission;

SUBMISSION 2: Comments on Reducing Pressure on Housing Affordability Measures (No.2); and

SUBMISSION 3: Comments on Foreign Acquisition and Takeovers Fees Imposition Amendment (Near- new Dwelling Interests).

SUMMARY

Foreign residents CGT exemption	Removal of the exemption may simply discourage foreign residents to sell their property in a market with rising prices, and thereby have an adverse effect on reducing the stock of vacant dwellings. Even if the amendment eases the general property market, the benefits may not be passed on to the renters.
Clarifying the principal asset test	The key features and the examples documented in Explanatory Memorandum are clear. However, the effectiveness of the amendment is questionable. A group of foreign residents can simply swap the membership interests in associates with direct interests in TARP assets.
Reconciliation payment	Requiring a reconciliation payment to be made by developers who sell dwellings to foreign persons will have minimal impact on housing affordability for first home buyers. This segment of foreign persons comprises a different market to that of the first homebuyers.
CGT discount on affordable houses	The increase in the discount from 50% to 60% is grossly inadequate to drive investment into sub market rental housing. We need an evidence-based approach to the level of incentives required and the distribution of those benefits between the investor and tenant outcomes.

SUBMISSION 1A

Treasury Laws Amendment (Reducing pressure on Housing Affordability No2) Bill 2017

Income Tax (Managed Investment Trust Withholding) Amendment Bill 2017

Submitted by National Affordable Housing Consortium (NAHC)

Sustainable Living Infrastructure Consortia (SLIC)

Griffith University

Prepared by Managing Director of NAHC – Mike Myers

Chairman of NAHC Board and Academic Leader of SLIC – George Earl

Griffith University Business School

EXECUTIVE SUMMARY

1. Submission

This submission is made by the National Affordable Housing Consortia and its research & development company, the Sustainable Living Infrastructure Consortia and includes working-party support from Griffith University.

2. Overall Summary

These proposals are part of the Commonwealth Government's "Comprehensive housing affordability plan for all Australians"

Whilst each of these 2 mechanisms are welcome there is no evidence presented, targets set or overall projected expenditure underpinning these two proposals to demonstrate what the expected outcomes will be for improving housing affordability.

Given the scale of the problem that the Commonwealth itself has documented, and the continued increases in households facing market exclusion or severe rental stress, the responses set out in the Exposure Draft are not designed to make a significant impact on the scale of the problem.

Having put its finger on two important issues, incentivising investment and facilitating more effective investment vehicles, the Government has failed to back either [and combine them] in a way that will deliver much substance to its 'Comprehensive housing affordability plan'.

CGT Discount

The increased 60% CGT discount sends a signal, but any basic modelling demonstrates that the increased benefit to investors is insufficient to make any significant impact for the tenant. How does it deliver real reductions in rent?

It may be that it can steer a bit of investment traffic towards CHP's, at the margins, that remains to be seen. It may be packaged with a range of other support, from the States etc but is that likely as it is not new supply and only has a 3 year timeline.

Ultimately, the benefit is so small and the likelihood that investors will capture 'all' of it as an offset to perceived target group 'risk', means there is likely to be no direct financial benefit transferred to the tenant.

MIT

Whilst it is understandable that the Government wishes to create a differential in the system to support the supply of *new affordable rental housing*, the Government is missing an opportunity to begin a much needed process to create an institutionalised segment of the private rental market.

Build to Rent creates the type of long term leasehold, tailored design, efficient ownership that is long overdue in the Australian private rental market but commonplace in comparative economies. The lack of action in support of growing that segment means supply side shortages will continue, putting further upward pressures on rents.

For decades policy makers have urged institutions to consider an infrastructure like approach to residential rental provision and a focus on long term running yield not capital gain, this Bill misses the opportunity to create MIT type arrangements to support investment at scale.

Such a shift would deliver wide and lasting community benefits, creating a 'fit for purpose' rental segment with strong new supply, long term tenancies & security for occupants and tailored models for market segments like retirees.

MIT as a mechanism for investment in affordable housing is welcome. However the expectation of delivering reduced rents at say 20% discount to market cannot be achieved through this mechanism.

Whilst the Commonwealth might expect States to provide the subsidy required, the track record is not good nor is it a recipe for certainty or scale or replicability.

Summary of proposed options that will enhance the effectiveness and scale of these affordable housing measures

CGT	*The increase in the discount from 50% to 60% is grossly inadequate to drive investment into sub market rental housing. We need an evidence based approach to the level of incentives required and the distribution of those benefits between the investor and tenant outcomes*
Diversity Mix [Stapling]	*20% of stock in an eligible MIT can be rented at market levels. This improves financial, social and risk management outcomes*
Capital & Depreciation Allowance	*Need adjusting to incentivise longer term holding and improved energy performance & sustainability*
All of Government structured support	*We proposed a package of supports which brings together commitment from each level of Government to underpin a model that can operate at scale and nationally*
Sovereign risk	*Measures to provide confidence are required*

3. Recommendations

3.1 The rules for MIT operations should enable a diversity of housing outcomes to meet different aspects of affordability. We recommend a rule that enables a maximum of 20% of dwellings in the MIT portfolio to be at market rents

Rationale: Diversifying tenant mix is acknowledged as contributing to inclusive communities. A measure of diversified income will reduce risk and enhance investment profile .It is likely that a diversified income stream will lead to better site selection that reflect the diversified tenants needs.

3.2 Treasury should work with stakeholders and leading research organisations to set out the policy statement and definition of 'affordable housing' for MIT to provide a framework that reflects locational, household and cost base factors but also provides some consistency and predictability. This should be approved through COAG treasurers and be included in the NHHA Multi-lateral Agreement

3.3 Community Housing Providers should not be required to consult State Government on a MIT Affordable Housing initiative, unless the State is a contributor of subsidy and support to that initiative

Rationale: We must avoid 8 different definitions and different benchmarks that will undermine confidence in the MIT and mitigate against institutional multi-jurisdictional investments. We also are wary of regular changes in State Government leading to a stop-start approach to housing policy. The issue of certainty for what will be long-term, expensive investments that require long lead in and high up-front costs needs to be considered. Examples abound.

If States are providing subsidy/land etc it is essential that the target groups, affordability and other outcomes are agreed with the State alongside the other investors. If States are not putting anything in, the requirement just adds red tape and indeed may operate as an effective veto. We oppose that that requirement.

3.4 The Commonwealth and States & Territories should work together to set out measures, preferably in legislation, that can enhance investor confidence in the MIT arrangements, including risks of retrospective changes, cancellation mid program and potential grandfathering 'safety net'

3.5 Each MIT should be able to elect to adopt the indexation method of calculation CGT liability or the Discount method

3.6 Where a MIT is providing dwellings at below 75% of the market rent and intends to do so for the minimum 10 year period [Annually reported], the MIT should be able to claim GST Input Tax Credits for each eligible dwelling

Rationale: This provides the kind of new supply incentive that helps set more effective and deeper rent discount rates. It is consistent with the GST tax treatment of charitable community housing providers who will be managing the projects and is expected to stimulate more supply into MIT

3.7 The Commonwealth and State & Territory Treasurers should set out agreed discounts or exemptions in Stamp Duty and Land Tax for MIT-Affordable Housing. These should be set out in the NHHA Multilateral.

The NHHA Multilateral should set out a common approach to Local Government Rate Relief for Community Housing Providers on all identified affordable housing managed dwellings, and such relief should be available on units supplied through MIT

3.8 To promote a supply of dwellings for longer terms than 10 years, the Commonwealth should enhance depreciation allowances for MIT units kept for 25 years. This means the structural elements of the building can be fully depreciated over 25 years

3.9 To promote sustainability and to reduce occupiers energy costs. MIT dwellings meeting an accredited rating [to be set under the MIT rules] will enjoy accelerated depreciation on the capital costs of eligible items that achieve the higher rating. [For example solar energy, customer and portfolio energy management systems, low energy appliances]

Yours Faithfully,	**Yours Faithfully,**
[redacted]	[redacted]
Mike Myers	**George Earl**
Managing Director	**Chairman of NAHC Board**
NAHC	**Academic Leader of SLIC**

Encl. : Detailed Report of this submission

SUBMISSION 1B

DETAILED REPORT OF THE SUBMISSION FOR

Treasury Laws Amendment (Reducing pressure on Housing Affordability No2) Bill 2017
Income Tax (Managed Investment Trust Withholding) Amendment Bill 2017

Background on the Submitter

This submission is made jointly by The National Affordable Housing Consortium (NAHC) and its subsidiary the Sustainable Living Infrastructure Consortium (SLIC) working in conjunction with the Griffith University Business School.

NAHC is a not-for-profit company registered with the Australian Charities and Not-for-Profits Commission. The objects of NAHC are to work with community groups, the private sector and governments to investigate, develop, promote and provide a range of innovative and quality affordable housing options to meet housing need.

Between 2009 and 2016, NAHC facilitated the construction of more than 3,500 affordable rental homes as an Approved Participant under the National Rental Affordability Scheme ('NRAS'). NAHC is the most successful NRAS Approved Participant in the country having delivered more NRAS affordable housing than any other organization, attracting $1.3B in private investment and saving tenants around $17m each year.

In 2012, the Company commenced a property management business exclusively for affordable housing, the Home Equity Rental Services (HERS). This business has grown rapidly and NAHC now manages over 1,000 homes from three offices (two in greater Brisbane and one in Townsville QLD).

NAHC are leaders in the research and development of new affordable housing and living approaches through its research arm dedicated to affordable housing known as the Sustainable Living Infrastructure Consortium (SLIC) which is active in national and State policy development in a number of areas including the provision of affordable housing for rental through the Managed Investment Trust (MIT) vehicles.

In depth applied research is currently being undertaken into MIT's in conjunction with the Griffith University Business School through the Department of Accounting, Finance and Economics and under the supervision of the chairman of SLIC Adjunct Professor George Earl.

NAHC has also established a company known as Buy Assist Australia Pty Ltd which has the dedicated purpose of providing shared equity home ownership solutions for people on moderate income who otherwise would not be able to purchase a home. This business is in a growth phase with the first 100 shared equity dwellings currently in delivery in the Melbourne market, with NAHC's equity leveraged through a $5m grant from the Victorian Government as part of Homes for Victorians announcements.

In 2016 NAHC and Places for People UK became associated companies and strong partners. Places for People group is one of the UK's largest and most successful property management, development and regeneration companies, a world leading organization with long term experience of shared equity and award winning social and affordable housing initiatives.

This partnership will enable NAHC's capacity to be scaled-up to make a significant contribution to housing outcomes in Australia, including our plan to establishment of a not-for-profit led managed Investment Trust for affordable housing. www.placesforpeople.co.uk/

Government Initiative

Currently, MITs are limited in their investment capabilities to passive investments, and cannot carry on or control an active trading business. The ATO has generally taken the view that any investment into residential property is active, with a primary purpose of deriving capital growth from increased value. This means that income from property investment through a corporate entity is generally not subject to the MIT concessions and is subject to tax at a rate of 30%.

We wish to applaud the Commonwealth on its initiative to use its powers to provide increased opportunity for investment in affordable housing through the two significant initiatives:

- a CGT incentive for investment in affordable housing by increasing the 50% CGT discount to 60%, and
- Making the concessional withholding tax treatment for fund payments to certain managed investment trust (MIT) members relating to affordable housing investment through MITs at the rate of 15%

The Commonwealth's proposal will allow MIT's to operate in the residential market subject to certain eligibility conditions, including;

- That the housing is for residential purposes (not commercial, hotels and the like)
- That the homes must be managed by a Community Housing Provider (CHP), providing the sector with a positive role
- That the homes are "affordable"
- That there is no overlap with NRAS incentives, and
- That the ownership is separate from the tenants who occupy the building

We thank the Commonwealth for the opportunity to make submission of the draft proposals and we would like to make the following comments.

There have been references to a requirement for a minimum of 80% affordable units in an MIT, however reading the current consultation drafts we can't see a reference to this and we take that it that 100% of the dwellings in the MIT must be affordable.

A residential MIT that consists of only of affordable housing, subject to the definition of "affordable", would include a range of rents and corresponding income profiles for tenants within a narrow band. There will be an upper cap of the band imposed by affordability policy, but there will also be a lower cap based on the capacity to pay rent without excess housing stress for tenants on low-moderate incomes.

These rents will need to be at a discount to market rents, and that will create a gap in the feasibility of an affordable build-to-rent project.

The financial benefits of having access to an MIT and the CGT benefit are obviously helpful, but on their own not sufficient to fill the feasibility gap for an MIT that consists only of affordable residential dwellings. In order to compete in the market place for development sites and resources, and to attract institutional investment there will be a need in almost all cases to a government subsidy, whether in cash, further tax relief, or the availability of land at below market value.

One strategy commonly used by affordable housing providers is for a project to contain a mix of properties, enabling the properties to be rented (or sold) across a spectrum of rents. The added value provided by the more expensive properties can be used to cross-subsidise the low and moderate value properties within the stapled group. This strategy could minimise or even eliminate the subsidy needed to achieve benchmark returns for investment in an MIT while also providing a substantial component of affordable housing.

There are social and financial reasons why it is better to have a range of demographic profiles in a mixed unsegregated environment over having a concentration of tenants who are all in similar circumstances in a particular location.

- Diversity creates the opportunity to match the housing needs of households to the available housing properties facilitating a housing career which can adapt to changes in family structure and age over time. Better matching between the type of housing that households need and the type of home that they occupy greatly increases the productivity of the housing stock.
- Investors will be more willing to finance for a project that has a diverse range of rent and product types because diversification lowers risk compared to a concentration of risk.
- There are direct social and economic benefits in having an inclusive community which contains a mixed range of incomes and demographics.

A good location for an affordable housing would be close to transport and services. This brings the opportunity to further value add to the project by providing some commercial development including retail and offices in the lower levels, and in some cases commercial carparking often below ground level. This strategy has a number of benefits, with the main one that the rents can contribute a disproportionately high amount of revenue to the overall development. There are architectural advantages to residents by elevating the lowest level of residential above the light and noise pollution of the street, and also the commercial space provides small business opportunities.

In advocating this approach, we are not proposing a departure from the core mission which is to provide affordable housing. We are proposing that it is better to use market processes to achieve outcomes where there is market failure, and that government subsidy should be the last not the first solution.

By creating a mixed environment, it makes the task of providing affordable housing within the project more financially achievable with either no subsidy or a subsidy lower than would otherwise be the case. The key is to design rules that ensure that the primary purpose of providing affordable housing is preserved as the central element, and that income derived from other uses is ancillary to the mission to provide affordable housing, even though the income from those ancillary uses might be significant.

Submission 1*: That the Commonwealth works with NFP providers to develop rules governing the composition of MIT's portfolios where, under the management of CHP's, a diversity of housing type and a diversity of mixed use is permitted while maintaining the primary purpose of if the MIT to provide affordable housing.*

The actual rents that will be paid and how these will be adjusted over time is an absolutely fundamental and critical input into the investment decision, and this is directly related to how 'affordability' is defined.

We understand that the definition of affordability will be determined by the relevant State where the project is located.

We submit that this approach is entirely unsatisfactory for the list of following reasons:

- If the States wish to participate by providing subsidy by way of grants or surplus land, then that would be a justification to include the State as a direct or proxy investor in the settling policy. However typically the States will have no direct interest in these developments, no role to play, and no checks and balances on their behaviour.
- States do not currently define affordability with serious investment by institutional investors in mind. The definitions lack an evidence based approach, and lack legal and academic rigour. States have responsibility for town planning policies implemented through Local Government and this leads to a hotchpotch of conflicting and confusing approaches to affordability. For example, Brisbane City the largest local government in Australia has provided generous infrastructure incentives for 5 star hotels but nothing for affordable housing.
- Leaving this important definition effectively to chance will lead to perverse outcomes not intended by the Commonwealth. The Queensland Government currently does not have a definition of affordable housing. The closest thing is definition of affordability currently used by the Queensland Government is the absurd policy found in Economic Development Queensland PDA Guideline No 16/2016 which sets affordability requirements within State Priority Development Areas. In the Bowen Hill PDA near the Royal Brisbane Hospital, the requirement is that 5% of rents must be no more than $640 per week. This exceeds actual market rents by 50%~70%. In 2016 the award salary for a second-year registered nurse in Queensland was $68,743. This means that a nurse would need to spend 48% of gross income to occupy one of the small number of "affordable" housing units required by developers in Bowen Hills. In the Mackay PDA rents can be as high as $726 per week and in Gladstone PDA $789 per week and qualify as "affordable".
- Institutional investors have an ingrained preference for a diversified portfolio. To attract this capital an MIT will ideally have properties in a number of States and locations. Given that the definition is fundamental to the calculation of investment return, having an ill-defined definition of affordability that is different in different locations is a significant barrier to investment.

Submission 2: *That the Commonwealth works with NFP providers and academic and research organisations to develop a workable definition and policy around "affordable" housing that is evidence based and subject to academic rigour, is suitable for the purpose of satisfying to expectations of institutional investors including regional adjustment, adjustment over time and achieving a balance between flexibility and certainty having regard to probity and the need for certainty.*

Submission 3*: That the definition and related policy should have regard to the requirements of investors, developers and State and Local Governments to the extent that they provide subsidy and support for affordable housing projects, but the central responsibility for implementing the affordable housing definition and policy should fall to the NFP proponent whose mission is the provision of affordable housing.*

Reference is made to a minimum investment period of 3 years. While it is appropriate to have a minimum period, the investment time frame envisaged is much greater than that, and subject to further work with institutional investors, could be 20 years minimum and is likely to be 30 to 40 years.

Over that timeframe investors will be very interested in assessing the level of sovereign risk.

The proposal in Submission 2 is intended in part to reduce the risk around how rents will be set now and in the future, and how the risk of a change in government policy at State or Commonwealth level could interfere with that process once the investment is locked in.

Thus, while the actions of future governments can never be known for sure, there are ways of structuring regulation that provides better comfort.

Submission 4*: That the Commonwealth works with NFP providers to review the legislative changes with the intent to reduce or minimise the perception of sovereign risk, including the risk of retrospective changes and grandfathering.*

The preceding sections discussed that the lack of housing affordability is result of market failure, and that after applying solutions that use market processes to minimise the gap between the market and the project, there will remain be in many cases a residual gap that requires government subsidy assistance for a residential project to attract capital investment and compete for resources in the marketplace.

These investment incentives should be considered in the context that there are changes in the areas of bank finance and taxation that will likely result in the reduction in the amount of property purchased for rental by small investors and SMSF's in the future. As Saul Eslake identified in his submission to the Senate Economics References Committee Enquiry in Dec 2013, a root cause of housing affordability failure is that the population is increasing faster than supply, and this has accumulated into a shortage of affordable housing. A barrier to the creation of residential build-to-rent in Australia, indeed affordable build-to rent, is that the yield is low compared to the requirement to attract institutional investment capital. (http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Affordable_housing_2013/Submissions)

We urge the Commonwealth to consider the submissions below aimed at increasing the operating yield of residential MIT's and therefore increasing the supply of affordable housing in the face of a contracting small investor market.

In relation to the 60% CGT beneficial treatment, our understanding is that (s 1.51) a capital gain of an individual that resulted from a CGT event occurring to units in a unit trust (including a MIT) that holds affordable housing will not qualify for an additional discount capital gain for affordable housing.

Submission 5: *Investors in a MIT should receive the benefit having the 60% reduction sale of property passed through at the end of the 30 or 40-year investment period as this would be a relevant consideration by an institutional investor.*

In fact, we are not satisfied with the current system of treating CGT because it is an unfair tax imposition on long term stable productive investment. The indexation method allows investors to gross up cost base of investment asset based on ATO index factor (CPI). With long term housing investment, in case housing escalation factor is equal or less than CPI (or ATO index factor), this method could make the cost base of the property less or equal the selling price, resulting in the reduction of net capital gain and minimise tax payable.

However, if the housing price goes up faster than average CPI, the investors will get more benefit by applying discount method in calculating capital gain.

Submission 5: *Complying residential MIT's should have the option to adopt the indexation method of calculating CGT liability*

GST is a major cost factor in development projects. Currently Input Tax Credits can be claimed where supplies by charitable institutions include rent at less than 75% of market rent. (Section 38-250(b)(i)) *A New Tax System (Goods and Services Tax) Act 1999* (Cth)).

Submission 6*: Given the mandatory role of the NFP in the management of the MIT management, we submit that the MIT be enabled to claim GST back, at least in proportion to the value of properties that are supplied at less than 75% of market rents.*

A problem for NFP organisations who supply property at below market rates to tenants is that the valuation process for Local Government rates and State Government Land Tax purposes generally does not recognise that that the property is supplied at less than full value. Thus the rents for affordable housing represent a higher effective taxation rate than the mainstream.

Further, because of the long investment period, the primary focus of the investment hurdle expected by institutional investors will be the yields during the operation of the MIT. Taxes such as rates, land tax and stamp duty act to increase the cost and thus the need for subsidy.

Submission 7*: Where affordable housing is provided by a residential MIT complying with the requirements, the rateable value of the property should be reduced proportionately for the purpose of calculation of Rates, Land Tax and Stamp Duty.*

Complying residential MIT's should be exempt from Rates, Land Tax and Stamp Duty to the extent that it provides affordable housing.

A New Type of Residential Product

In this final section we comment that they type of residential rental property that is proposed has some significant differences to the homes that are currently built and sold for rental by investors.

Currently in the mainstream tenants are denied the opportunity to make a property their home. They cannot choose interior colours or finishes, their lease is generally short term, even simple things like hanging pictures on walls and keeping pets can be a contentious issue with landlords, and at any one time a surprising number of urgent repairs are not attended to. Buildings are built to a price that may well leave the tenants with high operating costs such as energy consumption bills and rents inflated to cover necessary capital upgrades.

With an MIT buildings will be built to purpose offering long term security to tenants and designed from the outset to suit tenant needs to a much greater extent than most mainstream projects. This philosophy is underwritten by the long investment time frame whereby the investor is interested in minimising total cost in use over time, and the mission driven motivation of the CHP to provide management that meets tenant's genuine needs and expectations. It is important that the buildings are well built so that they can be properly maintained in the face of rents which are deliberately reduced to achieve the affordability outcomes.

This is not a cosmetic issue. The extreme case is the London fire where one of the issues was that fire escapes were not operational in a fire because the fire doors were kept open because the lifts in the building had broken down, and apparently no money fix them, and tenants had to use the stairs.

Submission 8: *Complying residential MIT's should have available accelerated depreciation on capital items to enable durable fittings, fitments and equipment to be installed. This will result in some savings to the ATO as the cost of maintenance expenses will be reduced.*

So that the building can be fully depreciated at the end of the term of the MIT investment, the depreciation allowance for the structural elements of the building should be increased so that the building can be depreciated over 20 or 30 years.

Submission 9: *Complying residential MIT's should have available accelerated depreciation on the capital cost of building elements that reduce the cost of energy use by the building over its life, including investment in passive architectural features, solar energy panels, energy monitoring and feedback systems, water tanks and other features provided that the design of the building achieves above mainstream standard in its environmental performance as accredited by a third part such as EnviroDevelopment of Green Star.*

We also comment that we would like to keep options available at the end of the investment period. Given that this is possibly 30 or 40 years into the future it would be desirable to have some flexibility. One option at that future time would be to sell the units to the residents, either fully or in shared equity.

That a caveat be placed on the requirement that the tenant does not have an interest in the MIT to provide for a transition-out phase of 3 years at the end of the investment period.

SUBMISSION 2

1. Removal of the main residence exemption for foreign residents

The removal of the main residence Capital Gains Tax (CGT) exemption for foreign residents may have the effect of increasing housing supply by inducing foreign residents to sell main residence dwellings. This, in turn, may have the effect of easing the supply/demand environment and perhaps reduce the stock of dwellings that are currently vacant. However, it is our view that the improvement in the affordability of dwellings in general, as a result of this proposed law change, will be marginal.

To the extent that the ownership of dwellings by foreign residents is concentrated on high density inner city areas, the impact of the proposed amendment on the general housing market would be quite limited. Even if the price pressure on the general housing market eases, this does not guarantee that tenants would receive the benefit of a reduction in rents. In addition, it is not clear whether the intention of the amendment is to remove the main residence exemption for taxpayers who are Australian citizens with an Australian domicile who become foreign residents for tax purposes during an overseas employment posting. While this is not directly related to the affordability of dwellings, would not the amendment affect the mobility of Australian citizens and who experience a temporary change to the tax residence status?

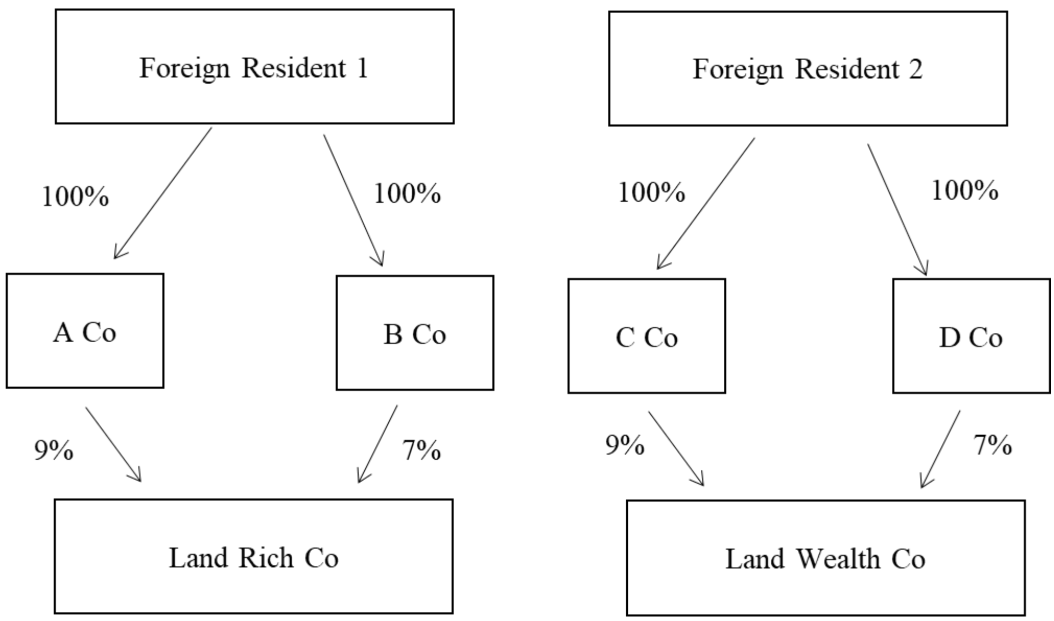
Furthermore, the impact of this amendment on reducing the number of vacant dwellings is questionable. If foreign residents are subject to CGT once they sell their main residence, especially in a market with rising prices, would they not be less inclined to sell the dwellings during their time overseas? This could have an adverse impact on the dwelling vacancy rate, which affects first-home buyers and renters. In addition, under a declining market, would this amendment not encourage foreign residents to sell the main residence to realise capital losses and thereby further depress the property market? Specifically, where a dwelling is a taxpayer's main residence, a capital loss from a CGT event happening to that dwelling is disregarded. Under the proposed amended law, the taxpayer would no longer be required to disregard such a capital loss and could use it to reduce their taxable capital gains.

a. Clarify the principal asset test is applied on an associate inclusive basis

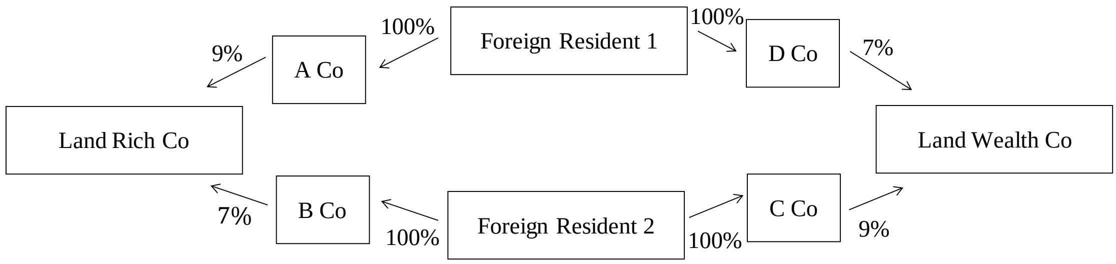
The key features and the examples documented in Explanatory Memorandum are clear. However, the effectiveness that the amendment will have on the affordability of dwellings is questionable. If there is a group of foreign residents, as explained in Example 1 (a) and (b) below (extending Example 1.8 in the Explanatory Memorandum), is there not a situation where the residents keep obtaining the CGT exemption even after the amendment is in effect?

Under the proposed amendment, the principal asset test (section 855-30) will be satisfied for both Foreign Resident 1 and 2 in Example 1 (a). However, by changing the holding structures of associates between Resident 1 and 2 (e.g. Resident 1 and 2 swap the holdings of B Co and D Co in Example 1 (a)), the principal asset test will be not satisfied (Example 1 (b)).

Example 1 (a):



Example 1 (b): After changing the shareholding structure (Resident 1 and 2 swap the holdings in B Co and D Co, respectively)



SUBMISSION 3

1. Require a reconciliation payment to be made by developers who sell dwellings to foreign persons under a near-new dwelling exemption certificate

A New Dwelling Exemption Certificate is issued by the Foreign Investment Review Board (FIRB) in respect of a development consisting of 50 or more apartments in order to provide pre-approval for a developer to sell to foreign persons. This avoids the need for each foreign purchaser to seek their own FIRB approval, which is an incentive for purchasers and streamlines the sales process for developers. Moreover, New Dwelling Exemption Certificates can be issued in respect of multi-storey buildings (i.e. apartments). Townhouses, house and land packages and greenfield developments are not eligible for New Dwelling Exemption Certificates.

Currently, the developer holding the New Exemption Development Certificate is liable to pay the applicable fee for each apartment sold to a foreign person. However, depending on the market, some developers may pass this cost on directly to the purchaser in full, or price a percentage of the fee into the adjustments for the sale of the apartment.

Hence, requiring an additional reconciliation payment to be made by developers who sell dwellings to foreign persons can be viewed in two aspects. Firstly, this amendment will tend to have a minimal impact on housing affordability for first homebuyers. Usually, the preferences for foreign investors are at the higher end of the market, which may be distinct from the part of the market that an aspiring first homebuyer is seeking to enter.

Secondly, if developers are able to pass on the entire amount of this additional cost, or even a portion of it, to foreign persons, this will result in price discrimination between foreign persons and local persons and might inflate the overall selling price of multi-storey buildings. As multi-storey buildings are usually located in high density, inner city areas, increases in multi-storey unit prices may trigger increased demand for detached housing in suburban areas. Such an outcome may not be conducive to increasing housing affordability.

2. Provide an additional affordable housing capital gains discount of up to 10 per cent if a CGT event occurs to an ownership interest in residential premises that has been used to provide affordable housing.

The increased 60% CGT discount sends a signal, but any basic modelling demonstrates that the increased benefit to investors is insufficient to make any significant impact for the tenant. How does it deliver real reductions in rent? It may be that it can steer a bit of investment traffic towards CHP's, at the margins, although that remains to be seen.

It would be more effective if there were an incentive scheme allocated to deliver affordable rents or reduction in rents rather than an increased in the CGT discount. The CGT discount is only applicable in the event of the eventual sale of the property. Given that such an event may occur many years after the initial decision to invest in an asset, the importance of the rate of the CGT discount to decisions about which assets to invest in may be overstated.

Ultimately, the relative benefit (between the proposed 60% CGT discount and the general CGT discount of 50%) is so small and the likelihood that investors will capture 'all' of it as an offset to a perceived target group 'risk', means there is likely to be no direct financial benefit transferred to the tenant.

Related to this point, it is noteworthy to focus on giving additional concessions to other housing related taxes such as; tax on land, stamp duty etc. to properties used to provide affordable housing.

RECOMMENDATIONS

1. To promote a supply of dwellings for longer terms, it would be more effective to offer an incentive scheme allocated to deliver affordable rents or reduced rents rather than the 60% CGT discount alone. The increase in the discount is grossly inadequate to drive investment into sub market rental housing.

2. Purchasing properties with New Dwelling Exemption Certificate prevents purchasers from seeking their own FIRB approval and its purpose is to intensify purchasers and streamlines the sales process for developers. However, if the introduction of this additional payment to the developer can be eventually passed on to the purchaser, this will create adverse impact on the overall housing affordability. Hence, it is recommended to closely monitor or impose a cap on a certain percentage that can be passed to the purchaser by the supplier.

Sincerely,

[redacted]

Mike Myers
Managing Director
NAHC

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George Earl
Chairman of NAHC Board
Academic Leader of SLIC