DomaCom
FRACTIONAL PROPERTY INVESTING

27th September 2017

Manager
Financial Services Taxation Unit
Corporate and International Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

via e-mail to: affordablehousingtax@treasury.gov.au

Dear Sir/Madam

Re: Increasing the supply of Affordable Housing

DomaCom Ltd (ASX.DCL) is pleased to make this submission as part of the public consultation process on the exposure draft legislation and explanatory material for Treasury Laws Amendment (reducing Pressure on Housing Affordability No.2) Bill 2017 and Income Tax (Managed Investment Trust Withholding) Amendment Bill 2017 announced jointly by The Hon Scott Morrison MP and by Hon Michael Sukkar MP on 14 September 2017.

DomaCom acknowledges the significant policy challenges confronting the Federal Government arising from the current crisis in housing affordability, and welcomes any initiative which legitimately plays a part in solving this intractable challenge.

However, the Company believes the legislation as proposed would perversely have the reverse effect for large sections of the Australian population. By prohibiting the acquisition of residential properties within Managed Investment Trusts (MITs) and thus reducing the supply of rental properties, the proposed legislation will, we believe, result in an increase in rental costs, further reducing housing affordability.

The proposed legislation will have a range of negative, unintended consequences including eliminating the domestic residential property trust industry in Australia. This appears contrary to a range of Government policy initiatives for the following reasons:

1. <u>Increased rental costs</u>

The legislation will increase rent costs by reducing the availability of rental properties, negatively impacting on housing affordability.

Globally, residential property trusts are responsible for creating a long-term supply of rental properties for people to occupy and it is well documented that Australia lacks this pool of long term rental stock. The proposed legislation will result in the elimination of residential property trusts within Australia, and it is difficult to understand this outcome would be desired by the government. MITs have been a well understood investment vehicle by investors for many decades and an appropriate vehicle for holding shares, fixed interest securities and real property including residential property as a means of long term savings for millions of Australians.

2. Discrimination against Gen X & Y and Millennials

These demographics will bear the brunt of reduced housing affordability while also eliminating their ability to get on the housing ladder by acquiring an interest in a property.

The Government is not banning investors from purchasing whole properties, therefore it is illogical to ban a structure which enables investors to acquire a percentage of a property, particularly given the current housing affordability crisis currently impacting Gen X & Y and Millennials. The ability to acquire a portion of a property is critical to facilitate property investment in this group allowing them to get on the property ladder at an earlier stage than would otherwise be possible.

3. Discrimination against middle income Australian investors

The current MIT tax regime treats equally investors who invest in ownership of part of a property as well as investors who purchase a whole property. Prohibiting domestic residential properties from being held within MITs unfairly discriminates against investors who invest in ownership of part of a property by denying them access to the tax benefits wealthier Australians enjoy while acquiring an entire investment property.

4. Erosion of the tax base

One of the benefits to Australia of having a residential property investment framework is that the income and capital growth derived from residential property is subject to tax in the hands of the investor. It is a tax transparent vehicle with all income passed through to investors. This income and capital growth is then assessed in their hands. By contrast, forcing younger Australians to purchase a property directly using significant amounts of leverage would place the property within the scope of the principal home CGT exemption which is exempt from tax.

5. Penalises domestic investors

The proposed legislation falsely assumes that MITs investing in residential properties are exploiting a tax loophole for the benefit of foreign investors. This is a fundamental misunderstanding of the make-up of investors who invest in residential property trusts. In the case of our DomaCom Fund, the reality is that the vast majority (96.9%) of investors are 'Mum and Dad' investors of which 99% are Australian and a large number are using their superannuation savings to invest in property through this mechanism.

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6. Mischaracterisation of the investment attributes of residential properties

The explanatory statements accompanying the proposed legislation state that investments in residential properties are not suitable "passive investments" for MITs such as shares because investors are primarily seeking capital growth rather than income. This assertion has no basis in fact – the return profile of residential property is very similar to equities in that some income (3-5%) and capital growth (5-6%) is delivered by both shares and residential.

7. Biased against a shared ownership model

The proposed legislation is negatively biased against the shared ownership model that is widely supported, including by the NSW Federation of Housing Association and Community Housing Providers (CHP).

DomaCom strongly supports initiatives in the legislation to drive the increased supply of housing for the affordable housing sector through the provision of increased incentives via improved capital gains tax outcomes. However this model only considers one part of the potential solution to the affordable housing challenge - increasing the supply of housing applicable for those to rent.

We feel it fails to consider the model championed by many CHPs which allows tenants who rent properties over time to eventually obtain equity in a property thereby creating a 'staircase' approach to increasing their equity in the home. The way the legislation is drafted a tenant and their associates would not be able to have an interest of more than 10% equity in an MIT. This will mean that those in the affordable housing sector will only ever be renters and are not provided with an incentive to create wealth through home ownership.

8. Penalises retirees

The proposed legislation will eliminate a new funding model developed by DomaCom that will enable retirees to release equity from their homes to fund their retirement while retaining ownership of the family home.

DomaCom has recently received in principle approval from ASIC for the relief instruments that will allow us to deliver a Senior Equity Release product to the baby boomer market that is fast running out of capital to fund its retirement. This global innovation uses the DomaCom Fund to fund the equity release for retirees. It overcomes the deficiencies which existed in many existing reverse mortgage products including by creating real transferability for the investor. The proposed legislation would stop this initiative in its tracks as it would ban the DomaCom Fund from investing in the residential properties owned by the retirees. Eliminating this product will increase the possibility of retirees falling back onto welfare as their savings run out.

9. <u>Penalises investment by Australian businesses</u>

The proposed legislation introduces a ban prohibiting MITs from investing in residential properties even before the legislation has been considered by Parliament and before the consultation process commences.

This is manifestly unfair and damaging to existing residential property trusts such as DomaCom, who made investments in good faith based on government policy settings. At a minimum, there should be an appropriate forward notice of the application of the proposed legislation so that stakeholders have the time to make any structural amendments to their business model and shareholders have time to consider what to do with their investment. It is difficult to understand any commercial rationale for the sudden introduction of changes of this nature.

<u>Background to DomaCom</u>

DomaCom Limited is an ASX Listed company which operates a registered Managed Investment Scheme that allows the holding of property assets within its scheme. DomaCom is part of a new wave of property crowd funding initiatives that has the potential to provide large scale solutions to housing affordability for younger generations as well as funding for retirees, and has a model for allowing those in the affordable housing sector to have a stepped approach to increase equity in their own home over time.

To date DomaCom has transacted approximately 50 times holding real property assets within its Managed Investment Scheme. Many of the property assets are residential properties from all states of Australia. They are typically in the price range of $300,000 to $500,000 and are off the plan which adds to the housing stock. The main investors (those that provide the capital) are SMSFs and individual investors that are sourced via the financial planning networks or directly invest via our web site.

DomaCom has developed its investment platform in Australia, employs local Australians and is providing a new and innovative online model for retail investors to obtain exposure to the property asset class including residential properties.

It is the Company's strong desire that the Government not damage innovation through legislation which considerably undermines its business and causes significant uncertainty for investors and shareholders.

Best Regards

Arthur Naoumidis

Chief Executive Officer
DomaCom Limited