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Future living for
Future thinkers

The Hon Dr Jim Chalmers
Treasurer

The Hon Julie Collins
Minister for Housing, Homelessness and Small Business

Director
Corporate Tax Policy Unit
Corporate and International Tax Division
Treasury
Langton Cres
Parkes ACT 2600

22 April 2024

Dear Treasurer,

Build-to-Rent Tax Concessions

Apt.Residential welcomes the opportunity to provide comments in response to the Treasury exposure draft legislation consultation paper regarding Build to Rent (BTR).

Apt.Residential is a specialist owner and operator of build to rent properties and invests the retirement savings of over 4.3 million workers in the healthcare and social services sectors from Europe.

Together with our capital partner, we were encouraged by Prime Minister Anthony Albanese's formal announcement made on 28 April 2023 to level the playing field for BTR and align withholding tax rates with all other commercial property sectors to 15%. On the back of the announcement, we have established an investment venture to deliver several thousand much needed new homes across Australia.

We are now extremely surprised by the sudden U-turn on the already announced policy which retracts most of the key measures that matter to the industry. These drastic and penalising controls create an enormous level of sovereign risk for offshore investors which have been a critical source of funding for our economy.

These measures are a clear barrier to investment and will undoubtedly divert capital away from our shores, they send a negative signal that Australia is not open for business and are contrary to supporting the addition of much needed housing supply in this country.

We urge the Government to honour its original commitment made last year and remove barriers to ensure the real estate industry can support the nation's quest to deliver 1.2 million homes over the next 5 years. We are currently tracking well short of those targets and, should the revised legislation be passed, it will undoubtedly increase the housing shortfall further impacting Australians from all walks of life.

The entire property industry, the largest employer in this nation, expresses its deep concerns with the adversely amended measures proposed which directly contrast with the promises made publicly by the Prime Minister and the purpose it seeks to address.

Further details are provided on these points and recommendations in this submission.

Should you wish to discuss any aspect of this submission, please contact the undersigned on matt.carolan@aptresidential.au.

Yours truly,

Matt Carolan

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Managing Director
Apt.Residential Pty Ltd

Executive Summary

Apt.Residential welcomes the Australian Government's engagement with the property industry on the evolution of BTR taxation settings. However, we have deep concern over the abrupt U-turn on the policy announced in April 2023.

The proposed measures come as a surprise and in direct contrast with the Prime Minister's announcement to remove tax impediments for BTR investing. The direct impact will be capital shifting elsewhere to countries which do not penalise institutional investment in BTR and where it can earn a superior return (as exemplified in markets such as The United Kingdom and The United States of America).

We have secured a substantial capital commitment from a global pension fund with encouragement following the Government's announcement last year. The uncertainty of these new measures present a direct risk to investment in Australian housing.

A permanent and perpetual solution with appropriate taxation settings is required to enable and facilitate incremental investment in the supply of housing in Australia. As a nascent industry, penalising the early movers which have taken the risk predominantly with the support of foreign capital, sets a negative precedent and increases the perception of sovereign risk in Australia.

The new proposed measures issued in April 2024 clearly set the property industry aback and made all parties worse off (less investment, less tax revenue, less employment, less housing supply, enhanced housing crisis lasting longer). These measures are the antithesis of promoting housing supply and stifle investment into Australia.

In summary, we believe the measures need to be amended as follows:

1. The reduced MIT withholding tax rate of 15% on rental income should not be limited to a period of 15 years. This is inconsistent with other comparable asset classes and should be extended to an unlimited period (provided the relevant requirements continue to be met).

2. The reduced MIT withholding tax rate of 15% should extend to capital gains (rather than be limited to rental income only). If required, the Government should give consideration to a 10-year minimum holding period to become eligible to apply the reduced 15% rate to capital gains.

3. If required, the Government should incorporate safeguards to prevent these BTR properties from being sub-divided and sold as individual apartments.

4. The affordable housing requirement to be eligible for these concessional BTR measures should be removed and instead addressed through a separate piece of legislation which adequately incentivises and supports the delivery of affordable housing.

Our Capital – Healthcare and Social Services Retirement Savings

Apt.Residential is a specialist institutional real estate group which owns, develops and operates BTR properties in Australia. We are supported by a large global pension fund which has been investing in our country for decades deploying several billion dollars, focusing to date on traditional office, logistics and retail property sub-sectors.

Our pension fund partner manages the retirement savings of over 4.3 million workers in the healthcare and social services sector, including many key workers and individuals from low and middle-income demographic groups.

Following the Prime Minister's announcement to reduce withholding tax rates for BTR in April 2023 and equalise the sector's treatment with all other types of commercial property, we have established a venture seeded with a large funding commitment by our pension fund partner to invest in institutional-grade BTR housing opportunities and improve outcomes in the Australian marketplace by contributing to the increase in housing choices. Our partner has been investing significantly in BTR markets globally though has only made limited inroads into Australia given the unfavourable tax regime up until the 2023 announcement.

The decision to start investing in Australian BTR was a clear signal by our pension fund partner in the conviction around the rental housing thesis and explicit acknowledgement of the country's deficit in this space.

The surprise announcement of 9 April 2024 by the Treasury however is a clear roadblock which deters commitments such as ours from progressing.

BTR as a Commercial Property Asset Class

BTR, or Multifamily as it is generally referred to in most other countries around the world, is categorised as a commercial property (not residential) asset class as it features many of the same key characteristics of other types of commercial real estate.

Investors are attracted to BTR investments due to the resilient long term cash flows generated by the asset class, it provides a lower volatility source of income helping support pension plan payments and retirement obligations of everyday workers.

This commercial classification is critical in understanding the role which BTR plays within institutional real estate portfolios of pension funds, sovereign funds and investors in Australia and globally alike.

It is unclear therefore why it is being associated with conventional residential for sale property which is a completely different sector from BTR. While we acknowledge the planning system in Australia lags the rest of the world in defining what BTR is, the taxation settings should not act as a barrier for the development of this industry which in places like the United Kingdom, Japan, Germany and the United States provides housing accommodation for millions of individuals and households thanks to the significant investment of institutional capital.

As you are aware, Australian superannuation funds are significant investors in BTR across Europe, the US and Japan having deployed billions of dollars. Superfunds have been attracted by the stable and supportive fiscal regimes which treat BTR equally to office, logistics, retail, hotels, student accommodation and many other commercial property sectors.

The key issue is the discrepancy in fiscal treatment of BTR relative to other property sectors in Australia. Apt.Residential is aligned with the broader property industry's advocacy for an even treatment of the sector and equalisation of the withholding rates to be set at 15% for income / distributions (on an ongoing basis rather than on a fixed 15 year time limited basis) as well as capital gains. Reverting to a 30% rate on capital gains will severely halt investors including ourselves and signal very clearly to the primary source of capital that Australia relies upon (i.e. offshore investors) for a functioning real estate market, that new housing investment is not welcome in our country. Our modelling indicates the impact to return on investment for BTR projects by increasing capital gains taxes alone to 30% is substantial and can be indicatively quantified in a greater than 150 – 200bps contraction in investment returns, rendering most projects commercially unviable.

Institutional BTR vs For Sale Residential (Strata Subdivision)

We emphasise the key characteristics of BTR, which as you are aware, include institutional in-one-line ownership, scale, professional management and security of tenure amongst others. It needs to be clarified that BTR does not foresee strata subdivision of properties and sell down to private individual investors.

Should a key driver of the proposed 30% capital gains tax regime be the Government's concerns with regards to risks of strata subdivision and circumvention of the incentives, we would support the inclusion of provisions or guardrails that would prevent this from happening and the recovery of tax liabilities from parties which undertake an asset's strata subdivision. BTR is a commercial asset class for long-term investing and should be treated no differently to the acquisition of an office or a warehouse property.

For noting, such guardrails are already in place at the State legislative level, as is the case in NSW for example, insofar as stamp duty and land tax considerations are concerned. Where a BTR asset is not being held in-one-line for a period of 15 years, the owner will be obliged to reimburse the office of state revenue any concessions granted over the entire period of ownership with penalties applying.

We reinforce the notion that BTR provides incremental investment into the broader housing market adding to the overall supply of residential accommodation, developing new stock and enhancing consumer choices. As an example, we recently acquired dated commercial assets to be redeveloped into BTR housing with no residential dwellings being withdrawn from the market through the process, and are in fact creating 291 new (incremental) dwellings with significant investment in the local community.

Australia Property Sector as a Net Importer of Capital

Australia is a net importer of capital and the Australian property industry relies heavily on patient, long-term global capital to finance major investments across property and social infrastructure. A competitive and stable tax regime is critical to ensure ongoing investment from major institutional investors such as pension funds and sovereign funds. You will be aware that these investors are typically tax exempt in their country of residence, therefore, any tax paid in Australia represents a real cost to them and a barrier to investment. Moreover, investments in many of these markets by foreign pension / super funds, sovereign funds and other qualified institutional investors are tax exempt and / or attract significant tax concessions which is in direct contrast with the penalising settings of this proposed BTR legislation.

Due to a variety of factors, investment returns in Australian real estate are amongst the tightest globally with countries such as the US, UK and Germany offering more competitive opportunities and therefore attracting a greater share of global capital flows. Therefore in such a competitive world where we are already challenged by the ability to offer returns aligned with larger and more liquid markets than Australia, any additional barrier such as a penalising tax regime for BTR will act as a clear deterrent for any investor considering supporting the development of more housing in Australia.

Groups such as Apt.Residential and our capital partner are genuine institutional commercial investors, we are adding supply to the housing market. Enabling BTR, as opposed to obstructing it, will provide more housing choices for Australians. Without making the relevant changes as outlined in this submission, the consequences are that more capital will continue to flow to other markets such as the UK and the United States as opposed to Australia.

Unfit Affordable Housing Provisions

A key area of concern relates to the proposed affordable housing obligations, while the intent and desired effects of these may be lauded, the application creates substantial practical challenges and adds more barriers to investing.

Firstly, any affordable housing inclusionary provisions should attract a lower withholding rate (for example 10% instead of 15%, as discussed in the EY analysis commissioned by the Property Council of Australia and submitted to Treasury in January 2024) in order to stimulate new investment. Affordable housing is largely an unviable investment in the absence of direct subsidies.

Secondly, we highlight the impracticalities of administering affordable dwellings in the form proposed by Treasury. There are a number of obligations imposed on landlords which are likely to cross privacy and other laws (for example how are tenant incomes and tax returns being monitored to establish eligibility criteria, how is that audited, what is the frequency of code compliance, which party bears the costs of administering this process etc.) rendering the proposal not implementable. There are several missing directives and details with respect to the landlord – tenant rights and obligations. Moreover, this policy absurdly punishes a key worker tenant which may receive a promotion or pay rise during his or her tenure within a property and which may as a result cross the income threshold due to their professional success in the workplace. We also note that there do not appear to be any “safe harbour” provisions in the draft legislation (as currently drafted) to allow for temporary non-compliance (due to circumstances described above). As a result, these affordable housing obligations create a real risk of penalising BTR operators due to factors outside of their control.

There are several other likely unintended consequences of what appears to be a not fit-for-purpose legislation which has not been properly considered by Government. We therefore urge all affordable provisions to be removed from the principal withholding tax settings and addressed through a separate piece of legislation which adequately incentivises and supports the delivery of affordable housing.